

REPORT
of the
ROYAL COMMISSION
on
DOMINION-PROVINCIAL
RELATIONS

BOOK I
CANADA: 1867-1939

BOOK II
RECOMMENDATIONS

BOOK III
DOCUMENTATION

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BOOK I

CANADA: 1867-1939 .

Rt. Hon. W. L. MACKENZIE KING, P.C., M.P.,
Prime Minister of Canada,
Ottawa.

Dear Mr. King,

I have the honour to transmit, herewith, the Report of the Royal Commission on Dominion-Provincial Relations, pursuant to the Order in Council of August 14th, 1937, P.C. 1908.

As noted in the final Chapter, the decisions underlying the recommendations of the Report were reached before the outbreak of war. The Commission has since reviewed its recommendations and, in spite of the great and relative changes in the financial outlook for Canadian governments, it believes its recommendations to be appropriate to meet the new strains and emergencies of war conditions.

I have the honour to be,

Sir,

Your obedient servant,

A handwritten signature in cursive script, appearing to read "J. G. Collins". The signature is written in black ink and is positioned above the printed name "CHAIRMAN.".

CHAIRMAN.

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NOTE.—The material contained in the research studies which have been published as Appendices (and which are listed on page 261) has been extensively used by the Commission in the preparation of Book I. It has not been thought necessary, however, to give exact citations or references to these studies except on occasion of actual quotation or long paraphrasing.

ROYAL COMMISSION ON DOMINION-PROVINCIAL RELATIONS

TERMS OF REFERENCE

PRIVY COUNCIL

CANADA

CERTIFIED to be a true copy of a Minute of a Meeting of the Committee of the Privy Council, approved by The Deputy of His Excellency the Governor General on the 14th August, 1937.

P.C. 1908

The Committee of the Privy Council have had before them a report, dated August 5th, 1937, from the Right Honourable W. L. Mackenzie King, the Prime Minister, submitting,—with the concurrence of the Minister of Finance and the Minister of Justice:—

1. That, as a result of economic and social developments since 1867, the Dominion and the provincial governments have found it necessary in the public interest to accept responsibilities of a character, and to extend governmental services to a degree, not foreseen at the time of Confederation;
2. That the discharge of these responsibilities involves expenditures of such a magnitude as to demand not only the most efficient administrative organization on the part of all governments but also the wisest possible division of powers and functions between governments. That particularly is this the case if the burden of public expenditures is to be kept to a minimum, and if the revenue-raising powers of the various governing bodies are to possess the adequacy and the elasticity required to meet the respective demands upon them;
3. That governmental expenditures are increased by overlapping and duplication of services as between the Dominion and provincial governments in certain fields of activity. That in other respects the public interest may be adversely affected by the lack of a clear delimitation of governmental powers and responsibilities;
4. That representations have been made on behalf of several provincial governments and by various public organizations that the revenue sources available to provincial governments are not in general adequate to enable them to discharge their constitutional responsibilities, including the cost of unemployment relief and other social services and the payment of fixed charges on their outstanding debt; that, consequently, if they are to discharge their responsibilities, either new revenue sources must be allotted to them or their constitutional responsibilities and governmental burdens must be reduced or adjustment must be made by both methods;
5. That representations have been made by provincial governments that municipal governments which have been created by, and derive their powers and responsibilities from, the provinces, are confronted with similar problems; that, in particular, necessary municipal expenditures have placed an undue burden on real estate and are thereby retarding economic recovery; also that the relations between provinces and municipalities are an essential part of the problem of provincial finances;
6. That, finally, it has been represented that unless appropriate action is taken the set-up of governmental powers and responsibilities devised at the time of Confederation will not be adequate to meet the economic and social changes and the shifts in economic power which are in progress without subjecting Canada's governmental structure to undue strains and stresses.

The Prime Minister, therefore, with the concurrence of the Minister of Finance and the Minister of Justice, recommends:—

1. That it is expedient to provide for a re-examination of the economic and financial basis of Confederation and of the distribution of legislative powers in the light of the economic and social developments of the last seventy years;

2. That for this purpose the following be appointed Commissioners under Part I of the Inquiries Act:—

The Honourable Newton W. Rowell, LL.D.,
Chief Justice of Ontario;

The Honourable Thibaudeau Rinfret,
Justice of the Supreme Court of Canada;

John W. Dafeo, Esquire, LL.D., of the
City of Winnipeg, Man.;

Robert Alexander MacKay, Esquire, Ph.D.,
Professor of Government, Dalhousie
University, Halifax, N.S.; and

Henry Forbes Angus, Esquire, M.A., B.C.L.,
Professor of Economics, University of
British Columbia, Vancouver, B.C.

3. That, without limiting the general scope of their inquiry, the Commissioners be instructed in particular:—

(a) to examine the constitutional allocation of revenue sources and governmental burdens to the Dominion and provincial governments, the past results of such allocation and its suitability to present conditions and the conditions that are likely to prevail in the future;

(b) to investigate the character and amount of taxes collected from the people of Canada, to consider these in the light of legal and constitutional limitations, and of financial and economic conditions, and to determine whether taxation as at present allocated and imposed is as equitable and as efficient as can be devised;

(c) to examine public expenditures and public debts in general, in order to determine whether the present division of the burden of government is equitable, and conducive to efficient administration, and to determine the ability of the Dominion and provincial governments to discharge their governmental responsibilities within the framework of the present allocation of public functions and powers, or on the basis of some form of reallocation thereof;

(d) to investigate Dominion subsidies and grants to provincial governments.

4. That the Commissioners be instructed to consider and report upon the facts disclosed by their investigations; and to express what in their opinion, subject to the retention of

the distribution of legislative powers essential to a proper carrying out of the federal system in harmony with national needs and the promotion of national unity, will best effect a balanced relationship between the financial powers and the obligations and functions of each governing body, and conduce to a more efficient, independent and economical discharge of governmental responsibilities in Canada.

The Prime Minister, with the concurrence of the Minister of Finance and the Minister of Justice, further recommends that the Honourable Newton W. Rowell, LL.D., Chief Justice of Ontario, be Chairman of the said Commission.

The Committee concur in the foregoing recommendations and submit the same for approval.

E. J. LEMAIRE,
Clerk of the Privy Council.

CERTIFIED to be a true copy of a Minute of a Meeting of the Committee of the Privy Council, approved by His Excellency the Governor General on the 18th November, 1937.

P.C. 2880

The Committee of the Privy Council have had before them a Report, dated 18th November, 1937, from the Right Honourable W. L. Mackenzie King, the Prime Minister, stating that the Honourable Thibaudeau Rinfret, Justice of the Supreme Court of Canada, has, owing to ill health, tendered his resignation as a Member of the Commission on Dominion-Provincial Relations, appointed by Order in Council of 14th August, 1937—P.C. 1908.

The Prime Minister, with the concurrence of the Minister of Finance and the Minister of Justice, recommends:—

1. That the resignation of the Honourable Mr. Justice Rinfret be accepted; and
2. That Joseph Sirois, Esquire, LL.D., of the City of Quebec, Notary Public, Professor of Constitutional and Administrative Law at Laval University, be appointed a Member of the said Commission, in the place of the Honourable Mr. Justice Rinfret.

The Committee concur in the foregoing recommendation and submit the same for approval.

E. J. LEMAIRE,
Clerk of the Privy Council.

CERTIFIED to be a true copy of a Minute of a Meeting of the Committee of the Privy Council, approved by The Deputy of His Excellency the Governor General on the 22nd November, 1938.

P.C. 2946

The Committee of the Privy Council, on the recommendation of the Right Honourable W. L. Mackenzie King, the Prime Minister, advise that Joseph Sirois, Esquire, LL.D., of the City of Quebec, a Member of the Commission on Dominion-

Provincial Relations established by Order in Council P.C. 1908 of the 14th August, 1937, be appointed Chairman of the said Commission vice the Honourable Newton Wesley Rowell, LL.D. resigned.

E. J. LEMAIRE,
Clerk of the Privy Council.

A. SKELTON, Esq.,
Secretary,
Commission on Dominion-Provincial Relations.

HISTORY OF THE COMMISSION

The Commission was appointed by Order in Council (P.C. 1908) dated 14th August, 1937, printed immediately preceding this section.

On August 31, 1937 Mr. Alex Skelton, chief of the research department of the Bank of Canada, was appointed by Order in Council (P.C. 2113) as Secretary of the Commission and Director of Research. Subsequently Miss M. K. Rowland was appointed as Assistant to the Secretary to aid in administration. Mr. Adjutor Savard was appointed French Secretary with particular responsibility for correspondence and relations with French-speaking Canadians. Mr. Savard acted as Secretary during the hearings at several provincial capitals and, in the later stages of the Commission's work, became responsible for the important task of supervising translation of the Report, appendices and other published studies. Mr. Wilfrid Eggleston was appointed Assistant to the Secretary with particular responsibility for supervision of reporting and travelling arrangements. After the public hearings Mr. Eggleston was transferred to the research staff of the Commission. Mr. R. M. Fowler of Toronto was appointed Registrar and Legal Secretary to the Chairman, Chief Justice Rowell, and after the retirement of the Chief Justice Mr. Fowler continued on the Commission's secretariat. Mr. Louis S. St. Laurent, K.C., of Quebec City and Mr. James McGregor Stewart, K.C., of Halifax, were appointed Counsel to assist the Commission in its public hearings, but except during certain sittings in Ottawa only one counsel was present at each hearing of the Commission.

Terms of Reference.—The Order in Council appointing the Commission imposed upon it a task of great complexity and magnitude. But wide and comprehensive as the terms of reference were, they were primarily concerned with one great problem, viz., the relations between the Dominion and the provinces. The Commission accordingly directed its inquiry strictly to this main problem. Many representations made to the Commission were concerned with other matters and, therefore, fell outside the scope of the inquiry.

The recital in the terms of reference set out certain conditions on which presumably the Commission was expected to report: the enlarged responsibilities of government due to economic and

social developments; the need for "the widest possible division of powers and functions between governments"; the allegation that expenditures were increased by overlapping and duplication of services as between the Dominion and the provinces; the complaint of the provinces that their revenue sources were inadequate to enable them to fulfil their constitutional responsibilities; the representations of the provinces that their municipalities were confronted with similar financial difficulties and, particularly, that conditions were such as to place an undue burden on real estate; and finally, the representation that unless appropriate action were taken, the governmental structure would be subject to undue stresses and strains in meeting the economic and social changes and the shifts in economic power which are in progress.

The operative clauses of the Order in Council more precisely instructed the Commission to make "a re-examination of the economic and financial basis of Confederation and of the distribution of legislative powers in the light of the economic and social developments of the last seventy years." Without limiting the broad scope of such an inquiry the Commission was instructed in particular:—

- (a) "*to examine the constitutional allocation of revenue sources and governmental burdens to the Dominion and provincial governments, the past results of such allocation and its suitability to present conditions and the conditions that are likely to prevail in the future;*"
- (b) "*to investigate the character and amount of taxes collected from the people of Canada, to consider these in the light of legal and constitutional limitations, and of financial and economic conditions, and to determine whether taxation as at present allocated and imposed is as equitable and as efficient as can be devised;*"
- (c) "*to examine public expenditures and public debts in general, in order to determine whether the present division of the burden of government is equitable, and conducive to efficient administration, and to determine the ability of the Dominion and provincial*"

governments to discharge their governmental responsibilities within the framework of the present allocation of public functions and powers, or on the basis of some form of reallocation thereof;

- (d) to investigate Dominion subsidies and grants to provincial governments.*

The Order in Council appointing the Commission clearly indicated that its task was two-fold: the Commissioners were instructed to consider and report upon the facts disclosed by their investigations; and "*to express what in their opinion, subject to the retention of the distribution of legislative powers essential to a proper carrying out of the federal system in harmony with national needs and the promotion of national unity, will best effect a balanced relationship between the financial powers and the obligations and functions of each governing body, and conduce to a more efficient, independent and economical discharge of governmental responsibilities in Canada.*" In short, the Commission was intended to be both a fact-finding body, and a body to make recommendations.*

Research Program.—In view of the many highly technical problems posed by the terms of reference the Commission decided in its first private meetings in September 1937, that it was impossible to fulfil its obligations by public hearings alone and that an extensive program of independent research should be carried on contemporaneously with the public hearings. This decision to engage research assistants was authorized by Order in Council (P.C. 2281) dated 15th September, 1937.

A comprehensive research program was accordingly organized and placed under the direction of Mr. Skelton, with Mr. J. J. Deutsch as Assistant Director. Broadly speaking, the program was grouped about three general heads: economics, constitutional matters, and public accounts.

The economic inquiry included such subjects of research as the economic background of Dominion-provincial relations, the national income, the financial history of Canadian governments, the economic effects of the Canadian taxation system, the role of municipalities and their relations to provincial governments, transportation, developments in Canada of services for social welfare, labour legislation. The following participated in research in economic matters:—

Stewart Bates, formerly Secretary of the Economic Council of Nova Scotia; Prof. George Britnell, Dept. of Political Science, University of

Saskatchewan; J. J. Deutsch, Research Department, Bank of Canada; H. Carl Goldenberg, Economist, Canadian Federation of Mayors and Municipalities, Montreal; Prof. A. E. Grauer, Director, Dept. of Social Science, University of Toronto; Prof. Paul-Henri Guimont, Dept. of Social Science, Laval University; R. A. C. Henry, formerly Deputy Minister of Railways and Canals; Joseph Howes, Assistant Director, Citizens' Research Institute of Canada, Toronto; Lawrence B. Jack, M.A.; Prof. F. A. Knox, Dept. of Political and Economic Science, Queen's University; C. T. Kraft, Ph.D.; Henry Laureys, formerly Director, Ecole des Hautes Etudes Commerciales, Montreal; Prof. Paul LeBel, Ecole Supérieure du Commerce, Quebec; J. C. Lessard, Economics Branch, Canadian National Railways, Montreal; Prof. W. A. Mackintosh, Head of Dept. of Political and Economic Science, Queen's University; Prof. Esdras Minville, Director, Ecole des Hautes Etudes Commerciales, Montreal; Prof. D. C. MacGregor, Dept. of Political Science, University of Toronto; Prof. Robert McQueen, Head of Dept. of Political Economy, University of Manitoba; Prof. J. L. McDougall, Dept. of Political and Economic Science, Queen's University; Stanley Nixon, specialist in public finance, Montreal; J. B. Rutherford, Dominion Bureau of Statistics; S. A. Saunders, Ph.D., author of several studies on the economic problems of the Maritime Provinces; J. C. Thompson, formerly Provincial Auditor of Alberta; Prof. François Vézina, Ecole des Hautes Etudes Commerciales, Montreal; Prof. W. J. Waines, Dept. of Political Economy, University of Manitoba; J. A. Walker, economist, Toronto; W. H. Wynne, Ph.D., formerly engaged by the Citizens' Research Institute in a special inquiry on taxation.

Research in constitutional and historical matters included studies in the legal interpretation of the British North America Act, certain aspects of other federal systems, the historical background of Confederation, the growth of governmental functions since federation, etc. The following participated in research in constitutional and legal matters:—

W. A. I. Anglin, K.C., Saint John, N.B.; Prof. D. G. Creighton, Dept. of History, University of Toronto; Prof. J. A. Corry, Dept. of Political and Economic Science, Queen's University; Harold E. Crowle, LL.B., Calgary, Alta.; Brooke Claxton, Montreal; L. M. Gouin, K.C., Montreal; Miss Kathleen Kearns, Ottawa; Prof. W. P. M. Kennedy,

* Italics in above paragraphs added.

Head of Dept. of Law, University of Toronto; and Vincent C. MacDonald, Dean of Law, Dalhousie University.

The Commission was fortunate in securing Mr. J. C. Thompson, F.C.A., formerly Provincial Auditor of Alberta, as Director of the Public Accounts Inquiry. Under Mr. Thompson's direction a financial questionnaire was prepared and sent to the treasury department of the Dominion and of each province. In general the Commission received whole-hearted co-operation from these departments, and comprehensive reports on a comparable basis of public finance for each province and the Dominion over the past twenty-five years were compiled. The Commission wishes to emphasize that this is the first occasion on which the statistics of public finance of all the provinces and the Dominion have been compiled on a comparative basis. These statements accompany the Report as Appendix 1.

Certain research studies which the Commission considered to be of permanent value and general interest have been printed as appendices to the Report. Other studies which were of less general interest have been published in mimeographed form. A number of special studies, many of them dealing with constitutional and legal matters, were prepared for the assistance of the Commissioners and not for publication. Copies of these will, however, be filed with the records of the Commission. It must, however, be understood that for facts or opinions stated in these reports, whether these reports are published or unpublished, the authors and not the Commission, assume full responsibility. A list of the printed and mimeographed studies appended to our Report is set out at the end of Book I.

Retirement of Mr. Justice Rinfret.—Unfortunately, before the first public session of the Commission, the Hon. Mr. Justice Rinfret was compelled to resign from the Commission on account of illness. The Commission desires to express its great sense of obligation to Mr. Justice Rinfret for his valuable advice and assistance in organizing the work of the Commission and in aiding in the selection of members of the research staff. His retirement from the Commission was a source of deep regret to his fellow Commissioners. Mr. Justice Rinfret's place on the Commission was taken by Dr. Jos. Sirois of the City of Quebec, Notary and Professor of Constitutional Law in Laval University, Quebec.

Public Hearings.—With regard to the public hearings, it was decided at the organization meetings of the Commission that public hearings should be held at Ottawa and at the provincial capital in each province unless some other city were designated by the province concerned. Public representations were to be limited to Provincial and Dominion Governments and to recognized public organizations, but the Commission reserved discretion to call any individual witness, if it saw fit. If municipalities desired to present submissions to the Commission it was stipulated that they should make arrangements through their provincial governments which would decide whether the municipal representations should be made by the government of the province or by the municipalities themselves. Conditions were laid down as to the form in which briefs were to be prepared and as to the time within which they should be filed. A general announcement in the press concerning the procedure at public hearings was made.

It was decided that before holding any public hearings the Chairman (Chief Justice Rowell), accompanied by the resident Commissioner wherever possible, and by the Secretary, should visit each provincial Premier and explain the general program and methods of procedure planned by the Commission. These visits were made in September and October, 1937, and all provincial Premiers without exception agreed to give to the Commission their full co-operation.

Public hearings were opened at Winnipeg on the 29th November, 1937. Between this date and the 1st December, 1938, hearings were held at all provincial capitals and at Ottawa, as follows:—

Place of Hearing	Dates	No. of Days
Winnipeg.....	Nov. 29, 1937 — Dec. 8	9
Regina.....	Dec. 9 — Dec. 17	8
Ottawa.....	Jan. 17, 1938 — Jan. 31	10
Halifax.....	Feb. 3 — Feb. 8	4
Charlottetown.....	Feb. 10 — Feb. 12	3
Ottawa.....	Feb. 15 — Feb. 16	2
Victoria.....	Mar. 16 — Mar. 25	8
Edmonton.....	Mar. 28 — Apr. 2	6
Ottawa*.....	Apr. 21	1
Toronto.....	Apr. 25 — May 9	11
Quebec.....	May 12 — May 16	4
Federicton.....	May 18 — May 23	5
Ottawa.....	May 25 — June 2	7
Ottawa**.....	Aug. 8	1
Ottawa.....	Nov. 24 — Dec. 1	6
	Total.....	85

* Evidence Dr. I. Jennings.
** Evidence Prof. L. F. Gihlin.

In the course of its public hearings the Commission recorded over ten thousand mimeographed pages of evidence, and 427 exhibits were filed. The Commission arranged for duplication and distribution of the evidence by its own staff in co-operation with the reporting staff, and by this means made its evidence available to the public at a lower cost than has hitherto prevailed, and succeeded (after supplying all the governments concerned with copies free of charge) in covering the total cost of reporting.

In addition to the briefs prepared by provincial governments, evidence of many departmental officials was taken for the purpose of investigating the alleged existence of overlapping and duplication between the services of the Dominion and provincial governments. One hundred and fifty-four briefs were received from municipal bodies and from public organizations. A list of exhibits indicating all governments and organizations which appeared before us is printed elsewhere.¹ The Commission also called a number of witnesses to deal with special phases of the inquiry. These witnesses include Dr. Heinrich Brüning, formerly Chancellor of Germany; Dr. Ivor Jennings, Reader in Law in the University of London, England; Dr. Gunnar Myrdall, Professor of Political Economy, Stockholm University, Sweden, and member of the Senate of Sweden; Graham Towers, Esq., Governor of the Bank of Canada; Dr. Roswell Magill, Under-Secretary of the United States Treasury; D. W. Bell, Esq., Acting Director, Bureau of the Budget, United States Government; Prof. L. F. Giblin, Professor of Economics, University of Melbourne, formerly of the Australian Grants Commission; and Bryce M. Stewart, Esq., Director of Research, Industrial Relations Counselors, Inc., New York City. Some of these witnesses were heard privately for the purpose of presenting confidential information. The Commission also consulted privately a number of other private individuals and officials.

Although in the preliminary visit made by the Chairman and the Secretary in September and October, 1937, the Premiers of all provinces expressed their willingness to co-operate in the work of the Commission, it was found that full participation by all provincial governments was not forthcoming. The Government of Alberta subsequently declined to appear before the Commission or to participate in its activities. The position of the Government was set forth in a letter from Premier Aberhart to the Chairman in reply to a request for the Government's views on various questions:—

¹ See Book III.

OFFICE OF THE PREMIER

ALBERTA

EDMONTON, March 30, 1938.

DEAR SIR,

Owing to the fact that the legislature has decided against presenting a brief to the Commission on the grounds already outlined to the Federal Government, we would respectfully suggest to you that it would be inconsistent and contrary to the decree of the legislature to answer the questions you have directed to us.

It is our intention to present a comprehensive brief directly to the Federal Government, a copy of which will be sent to each of the provinces.

Yours truly,

(Sgd.) WILLIAM ABERHART,
Premier.

HON. NEWTON W. ROWELL, Chairman,
Royal Commission on Dominion-Provincial Relations,
Edmonton, Alberta.

The Commission also inquired if the Government had any objection to its summoning various officials to appear before it to give evidence on the matter of overlapping, but the Premier objected in view of the resolutions of the Legislature.² At the hearings in Edmonton the Edmonton Chamber of Commerce, however, presented a comprehensive survey of the position of the Province within federation, and thereby a serious gap in information was avoided.

The Province of Quebec was represented at the opening session of the hearings in Quebec City by counsel who welcomed the Commission and presented a memorandum setting forth its reasons for not participating. The memorandum declared in part:—

"... nous devons déclarer que le gouvernement de la province de Québec ne comparait devant cette Commission, ni en qualité de demandeur, ni en qualité de défendeur; et qu'il n'entend être lié en aucune façon par les conclusions de votre rapport.

Si le gouvernement de Québec a cru devoir se faire représenter à cette séance initiale, c'est qu'il n'a pas voulu manquer de courtoisie envers la Commission; c'est aussi parce que son silence aurait pu être considéré comme un acquiescement au principe qu'a posé le gouvernement fédéral, en confiant à une Commission nommée par lui seul la mission de faire enquête en vue d'amender l'acte fédératif de 1867."³

² Ev. pp. 6225-26.

³ Ev. pp. 8130-31. Provincial translation.—"... we beg to state that we are not appearing before your Commission either as an applicant, nor as a defendant, and that we shall not feel bound, in any way whatsoever, by the opinions contained in your report.

The Government of this Province is appearing before you because, in the first place, it did not wish to be lacking in courtesy towards this Commission, and also because its silence might have been construed as an acquiescence in the principle laid down by the Federal Government, in appointing, of its own accord and without consulting the Province, a Commission whose report might form the basis of possible amendments to the Constitution. . . ."

The Government of Ontario co-operated fully in supplying the Commission with statistical information, and in public hearings at Toronto, with the exception of answering a number of questions addressed to the Government by the Commission, but later declined to co-operate further, alleging that there had been a breach of faith on the part of the Dominion Government which had changed the gift tax section of the Income War Tax Act prior to the Report of this Commission.⁴

Retirement of the Chairman, Chief Justice Rowell.—To the great regret of his fellow Commissioners, the Chairman of the Commission, Chief Justice Rowell, became seriously ill in the early part of May, 1938, and was unable to attend the public hearings in Quebec and Fredericton. For a time it was hoped that the Chief Justice would recover sufficiently from his illness to permit him to resume his work with the Commission. When it was found that this was impossible the Chief Justice's resignation as Chairman was tendered to the Dominion Government. After a lapse of several months the Dominion Government felt compelled to accept Chief Justice Rowell's resignation and Dr. Jos. Sirois was appointed Chairman, but no new member was added to the Commission.

The illness and retirement of the Chief Justice was to each of us a great personal loss, and we bear tribute here to his fineness of mind and character, his courtesy, patience, and consideration, which made working with him a pleasure and a privilege. As Chairman he guided the planning of the research program and arrangements for final hearings, and he took an active part in the supervision of the research program up to the time of his illness. He presided at the public hearings in seven of the nine provinces. His great knowledge of Canadian affairs and of constitutional law, his long experience in public life and private business, his courtesy, tact and precision of mind, were of inestimable value both in the conduct of the public hearings and in the private deliberations of the Commission. We deeply regret that it was impossible for Chief Justice Rowell to participate in the preparation of our Report, and he is not in any way responsible for the conclusions which we have reached.

Final Hearings.—During our hearings in provincial capitals it had been indicated to the provinces that an opportunity would be given to them to make supplementary representations replying to

the contentions of other provinces and of reviewing the research studies. Arrangements were made for final hearings in Ottawa after the provinces had time to consider each other's evidence and the research material prepared for the Commission. With regard to the research studies the Commission wished to give the provinces and the Dominion full opportunity to examine and criticize them before they were put in final form or used for purposes of the Report. Accordingly, draft copies of the research material as completed were sent to the Dominion and all provincial governments which signified their desire for them (among them Alberta). Final hearings were held in Ottawa from November 24th to December 1st, 1938. The Governments of British Columbia, Manitoba, New Brunswick and Prince Edward Island were represented, and various supplementary representations were made on their behalf. (The representations of Manitoba were supported by Saskatchewan, while Nova Scotia made certain comments to the Commission in writing.) In addition, some of the research material was discussed at length. Comments on the research material, whether during these hearings or by correspondence later, were given careful consideration.

The fact that the Dominion Government and several provincial governments did not appear at our final hearings somewhat altered the character of our inquiry. Our task was, however, to some extent simplified though not abbreviated. We were obliged to continue with our inquiry without having to consider how far our proposals would be acceptable to any of the ten governments.

Form of the Report.—The form of the Report was naturally of much concern to the Commission, but after due consideration it has arranged its Report to correspond roughly to the nature of its task. As already pointed out, the Commission was both a fact-finding body, and a body to make recommendations. For convenience it has accordingly kept its recommendations separate in the main from the detailed data on which they are based. Book I of the Report represents a "pooling" of the research work of the Commission's expert staff into the economic and social developments of the past seventy years and their bearing on the working of the federal system. Book II consists of recommendations based upon the evidence submitted in public hearings and the facts disclosed in Books I and III and in special research studies. Book III consists largely of relevant statistical data including summary statements of the Commission's exhaustive inquiry into Dominion and provincial

⁴Letter, dated July 13, 1938, from Hon. M. F. Hepburn, Premier of Ontario, to the Secretary, enclosing correspondence between Mr. Hepburn and the Prime Minister of Canada.

public accounts, summary statements of municipal finances, and statistical statements illustrating in detail the Commission's financial proposals contained in Book II. It should be fully understood, however, that all three Books are part of a single report which has been bound in separate volumes merely for convenience. In addition to the Report proper, for which the Commission must take full responsibility, it may be noted again that the Commission has published in addition a number of its special research studies which it believes to be of general interest and relevant to the Report. For these research studies the Commission, of course, does not assume responsibility.

Although the Commission did not have the benefit of any representations from the Dominion Government it received full co-operation and assistance from every official of the Dominion services from whom it requested information. At the request of the Commission a number of deputy ministers, assisted by members of their staffs, appeared at public hearings in Ottawa and gave valuable information concerning the work of their departments. In addition, much information, statistical and otherwise, was prepared for us by these and other officials in answer to private inquiries. To all these officials we express our appreciation for their patience and co-operation, and it will not be inappropriate to mention the following who gave us special assistance: Dr. R. H. Coats, Dominion Statistician; Mr. C. Fraser Elliott, K.C., Commissioner of Income Tax; Mr. H. Marshall, Dominion Bureau of Statistics; Miss Margaret Mackintosh, Department of Labour; Dr. A. K. Eaton, Department of Finance; Mr. V. C. Phelan, Department of Labour; Mr. J. R. Beattie and Mr. J. E. Coyne of the Research Department of the Bank of Canada.

Particular mention must be made of the able and willing co-operation which the Commission received from the staffs of the Bureau of Translation and the King's Printer, who were required to work under great pressure and for long periods of overtime in the final stages of the preparation of the Report.

We desire to express our appreciation as a Commission and as individuals for the courtesy and hospitality which we have received in all parts

of Canada. We thank especially those organizations which submitted briefs, and those officials and individuals who gave generously of their time and ability to provide information which the Commission required from them. The arrangements made by all provinces for the conduct of the hearings left nothing to be desired, and the general spirit of co-operation shown by provincial governments, municipalities and organizations which appeared before us was of great help to us in our difficult task.

The Commission also wishes to record its appreciation of the services and the fine spirit of co-operation of its secretariat, its research, reporting and clerical staffs. In particular it would mention the work of Mr. Skelton, who carried the dual load of administration and direction of research; of its other secretaries, Mr. Savard, Mr. Eggleston and Mr. Fowler; of Mr. J. C. Thompson who directed the Public Accounts Inquiry and Mr. J. A. Brennan, C.A., his principal assistant; of Miss Rowland and Mr. Deutsch who acted as Mr. Skelton's principal assistants in administration and the direction of research respectively; and of Professor Corry and Professor Creighton who assisted in co-ordinating research material. The research program of the Commission was the most comprehensive ever undertaken in Canada in a public inquiry. The Commission hereby records its appreciation of the excellent work done by its research staff, many of whom served at personal inconvenience and sacrifice. To its official reporters, Messrs. Oliver and Hubbard, the Commission's thanks are due both for the consistently high quality of their work and for their co-operation in making possible the very economical reporting. To the clerical staff, who were prepared to work at all hours and often under material conditions far from ideal, the Commission is deeply grateful. In this connection it wishes to mention the work of Mr. W. J. McHugh who was in charge of the enormous task of mimeographing the evidence and the studies; and Miss Mary White and Miss Rachel Fortin who acted as personal secretaries to the Commissioners.

Finally, we thank the press of Canada for their full and careful reporting of our proceedings; and for the informed, constructive comment and criticisms which they offered as the work of the Commission proceeded.

CHAPTER I

CONFEDERATION

1. THE FORCES LEADING TO CONFEDERATION

Canadian Confederation was a great political achievement. It was made possible by a remarkable conjuncture of events which brought each of the separate colonies to a crisis in its affairs at the same time and pointed to political union as a common solution of their difficulties. Great Britain, for the time being disillusioned with empire, had reversed the military and commercial policies which had sheltered and nourished the colonies in the past. The loss of the imperial preferences had compelled all the colonies to face drastic readjustments. In the Province of Canada, this disaster coincided with the final failure of the costly St. Lawrence transportation system designed to tap the trade of the Middle West. The public finances of the Province were seriously involved in the failure of this ambitious venture at the very moment when the strife between Upper and Lower Canada had led to a political impasse. In the Maritimes, the nicely balanced economy based on the sea was threatened by the new agents of steel and steam; an onerous public debt had been incurred for railways and the loss of the imperial preferences was a heavy blow. These circumstances provided tribulations enough for colonial statesmen; in addition there was the hostile attitude and aggressive expansion of the United States.

The territorial aggrandizement of the United States impelled a defensive political union of the British colonies in North America. The loss of imperial preferences and probable withdrawal of trading privileges by the United States gave point to arguments for economic union. The railways, lately come to North America, provided for the first time a means of uniting vast continental areas under a single government. In a larger union, there might be not only an escape from present and impending misfortunes but also a brighter future. Out of the failures of the past, the perils of the present and the hopes for the future, there emerged a new purpose and design for British North America. It not only required that there should be union but also decided largely the form it should take. The purpose, the original structure and much of the subsequent history of the Canadian federation find their explanation in the very factors which brought union about.

The American Revolution left half the continent with two tiny pockets of settlement under the British flag. These two pockets had developed into four self-governing colonies, and struggling settlements had gained footholds in the western wilderness and on the Pacific Coast. The older colonies had matured greatly, both politically and economically, but, being essentially dependent on water transportation, they had remained isolated from one another. As British dependencies, their economic development had been shaped by the imperial commercial system. They thought in terms of external rather than British North American trade.

The Maritimes looked to the sea. They concentrated on their timber and fish, their ship-building and their carrying trade. Their own hinterland and the vast continent behind them were little in their thoughts. The Canadas had developed a thriving export trade in timber and wheat. The most active spirits, however, took these outlets for granted and faced inward on the continent. For them, the St. Lawrence water system was not so much a political boundary as a great highway leading into the heart of the continent. From the beginning, the Canadians had dreamed of a future when a trade of continental proportions would pour along their highway. The other British colonies had little place in their plans for the St. Lawrence as one of the great trade routes of the world. And the concerns of the Red River and Pacific Coast settlements were entirely foreign to those of Canada and the Maritimes. The separate pre-occupations of the colonies had led them in opposite directions emphasizing, in social terms, their physical isolation from one another.

Thus, in spite of their growth, the British colonies in North America had remained small and isolated pockets of settlement. They had grown up in reliance upon the mercantile privileges supplied by the British navigation laws and trade preferences. This was their world and they would be compelled to find an entirely new scheme of existence if it disappeared. And disappear it did in the two decades before Confederation. By adopting free trade at home, Great Britain swept away the privileges on which the provinces had relied. With the grant of responsible government,

imperial control over colonial fiscal policy was relinquished. The imperial authorities insisted that responsible government carried with it the responsibility for defence and the colonies were notified that the garrisons would be withdrawn. The threatened recall of the legions marked the end of the sheltered world the colonies had known.

Accustomed to shelter, the first reaction of the Province of Canada was to seek a new privileged relationship with the United States. This movement which resulted in the Elgin-Marcy Reciprocity Treaty of 1854 met with some short-lived success but the permanence of any such solution soon became open to the greatest doubt. Unfortunately for the peace of mind of the colonies, the change in British imperial policy coincided with the rise of continental imperialism in the United States.¹ During the fifties and sixties, the far west was rapidly organized into territories under the aegis of the United States. The projection of transcontinental railroads by American promoters aroused deep alarm in the minds of British North American statesmen.² Aided by new methods of settlement³ and transport, settlers were swarming westward and eddying northward towards the domain of the Hudson's Bay Company.⁴ This quick advance across the continent was accompanied by hymns to "manifest destiny" and by repeated, though largely irresponsible demands for the annexation of the British colonies to the north. Even if Canada and the Maritimes were not seriously threatened, it became increasingly doubtful whether the United States could be prevented from swallowing the rest of the continent, including the territories of the Hudson's Bay Company and the feeble British settlements on the Pacific Coast.

The American Civil War with its border incidents and its Anglo-American disputes intensified the alarm, and anger at Great Britain ensured that the United States would abrogate the Reciprocity Treaty at the earliest opportunity. The "Alabama claims" were translated into a demand for territorial compensation. Various threatening gestures were made by the American Union which emerged from civil war as one of the great military powers in the world. In the early sixties, the era of peaceful political relations and advantageous commercial arrangements with the United States

appeared to be definitely over. The political independence of the colonies was insecure and their material prospects were discouraging in the extreme. They had lost their most valuable commercial privileges in the retreat of one empire and they had no hope of countervailing advantages from the threatening advance of another.

The abrupt reversal of British policy and the rapid expansion of the United States were events of world-wide significance. Either of them taken singly would have been a heavy blow to the provinces. Their coincidence intensified this pressure and gave it an urgency it might otherwise have lacked. Had Britain retained the old commercial system, the provinces might have remained uneasily passive in the face of American expansion. If their southern neighbour had shown herself pacific and eager to trade on advantageous terms, they might have permitted themselves to be drawn quietly and separately into her orbit. As it was, these events were loosed upon them in the same period, forcing them to contemplate radical measures. They began to see solid advantages in a political union which had never hitherto been seriously entertained. Through a united front, they might hope to resist the northward expansion of the United States. By organizing trade among themselves, they might compensate for the loss of their valuable commercial privileges.

There were a number of factors in their domestic situations which urged drastic action and also pointed to the same solution. The long efforts to draw the trade of the mid-continent down the St. Lawrence had met with final failure. The public debts incurred for railways and other improvements of the St. Lawrence transportation system had almost destroyed the credit of the Province of Canada in the London money markets. The possibilities of further expansion within the Province were severely limited and vigorous commercial groups in Montreal and Toronto, disappointed over the failure to tap the Middle West, were looking for new fields for enterprise. In these circumstances, attention turned increasingly to the possibilities of the North-West. The imperial authorities were willing for Canada to take over Rupert's Land. As long as everything depended on water transportation, it had not been commercially accessible. But the coming of the railways seemed, for the first time, to open the way for its development. South of the boundary, the United States was showing how railways could be used to organize a continental domain. With the aid of this new technique, Canada might duplicate the impressive

¹ Texas was annexed in 1845, Oregon in 1846, and Alaska purchased in 1867.

² The Union Pacific was chartered in 1862 and the Northern Pacific in 1864, the latter being frankly planned as an international transcontinental road.

³ In 1862, the Free Homestead Act opened the American West on most advantageous terms to incoming settlers.

⁴ Minnesota, which lay just south of the tiny Red River settlement, was admitted to the Union in 1858.

expansion of the United States. As an escape from the disappointments of the past and the hampering limitations of the present, the attractions of a national transcontinental system became ever more compelling.

The pressure for expansion to the West came mainly from Upper Canada, seething with the typical urges of frontier America. This fact had a disturbing influence on the unstable political union of Upper and Lower Canada. In spite of the unitary form of the constitution established in 1841, the Province of Canada had taken on the main features of a federal system. The Act of Union had awarded each section an equal number of representatives in the provincial assembly, and the practice of dividing ministerial posts and votes of public money fairly equally between them maintained an uneasy political balance between French-speaking and English-speaking Canadians. The instability of this equilibrium became more marked as the population of Upper Canada outgrew that of Lower Canada and the former demanded increased representation which would reflect its decisive superiority in numbers. The union thus endangered the cultural heritage of Lower Canada. Annexation of the Northwest, leading to further British settlement, would involve a westward transference of the provincial centre of gravity. Lower Canada would be doomed to political subordination, and the threats to its cultural values were intensified.

French Canada would not acquiesce in the swamping of its own way of life and the collapse of the Taché-Macdonald Government in June, 1864, after only three months of office, clearly revealed the impasse to which Canadian politics had been brought. The coalition which succeeded it was frankly formed to explore the possibilities of federal union, either of the Canadas alone or of British North America as a whole. In the Province of Canada, internal political deadlock and financial stringency intensified the pressure for a sweeping adjustment.

At the same time, the vision of transcontinental expansion had begun to have some attraction for the Maritimes. They were suffering from the loss of their protected markets and the new techniques of the industrial revolution were disturbing their habitual pursuits. Steam-driven vessels were overhauling the famous clipper ships and cutting into the carrying trade of the Maritimes. These circumstances led them to consider seriously the possibility of closer relations with Canada. Here

again it was the railway which brought this possibility within the realm of the practical. New Brunswick and Nova Scotia had strained their public finances to build railways which were as yet incomplete. But the completion of the Intercolonial would, it was thought by many, bring the commerce of Canada into the ice-free ports of Halifax and Saint John. With a little optimism they could see the trade of a transcontinental British North America canalized in the same way. And for the Maritimes too, the growing belligerence of the United States darkened the horizon, and intensified the Maritimes' recognition of their own inability to protect the fisheries.

Thus the pressure for union grew out of the circumstances of the colonies. The nature of these circumstances, both economic and political, determined the character of the union. The political conditions are familiar and need no further discussion. The economic conditions influenced greatly much of the framework and detail of the federal scheme. To grasp the design of the architects of Confederation it is therefore important to look more closely at the economic and social conditions of the time.

2. THE ECONOMY AT CONFEDERATION

About three and a half million people lived in the British North American colonies at the time of Confederation, three-quarters of them in the Province of Canada. Four-fifths of the total population was rural. Montreal, much the largest city, had about 100,000 population.⁵ Most people were engaged either in cultivating the soil or extracting raw products from the forest and the sea. These principal occupations supported a small group of manufacturing, handicraft and service industries, widely scattered through the settled areas. These industries were sheltered from foreign competition, partly by natural advantages such as local abundance of cheap raw materials and the lack of transportation facilities and partly by the incidental protection of a revenue tariff. The percentage distribution among the various occupations is shown in Table 1 on the following page.

⁵ Quebec with 60,000 and Toronto with 50,000 were the only other towns boasting more than 30,000 population. Barely 12 per cent of the total population lived in towns exceeding 5,000.

TABLE I.—OCCUPATIONS OF THE PEOPLE, PERCENTAGE DISTRIBUTION, 1871⁶

	Ontario	Quebec	New Brunswick	Nova Scotia	Total
	%	%	%	%	%
Farmers, lumbermen and fishermen.....	51	52	51	52	51
Manufacturing and handicrafts.....	14	11	12	10	13
Construction and unskilled labourers.....	18	17	18	15	18
Miners.....				2	
Sub-total.....	83	80	81	79	82
Services*.....	17	20	19	21	18
Total.....	100	100	100	100	100

* Includes wholesale and retail trade, transportation and communication, government and education, finance, the professions and personal services.

The self-sufficiency of separate families and of small isolated communities—in short, the rural and frontier nature of the economies as a whole—is illustrated by the relative unimportance of the service occupations. A complex, highly specialized, metropolitan society requires a highly developed system of services.⁷ In the Canada of today, about forty per cent of the gainfully occupied are engaged in supplying services rather than in producing goods, compared with eighteen per cent at the time of Confederation. The extraction and crude processing of natural products then absorbed the energies of most of the population.

The Maritimes—dependence on wood, wind and water techniques

The economy of the Maritimes was based on the forest and the sea. Fishing, lumbering, shipbuilding and the carrying trade were the principal occupations. Table I indicates that farming, lumbering and fishing accounted for over half of those gainfully employed in New Brunswick and Nova Scotia. As the numbers who made farming a full-time occupation were not large, the overwhelming importance of the forest and the sea is clear. The Maritimes had grown up as a part of the old British commercial system which sought to make the Empire a closed trading unit, and they had responded to the demands of that policy. Fish had long been one of the great staples which the colonies were encouraged in various ways to

⁶ These percentages are derived from the census of 1871 and may be taken as approximately correct for 1867.

⁷ That is, occupations which are not concerned with the direct production of goods, such as wholesale and retail trade, transportation, banking, the professions, etc.

produce. Indeed, the rise of Nova Scotia was, in a measure, due to the protected markets for cod in the West Indies which were partly lost by the New England fishermen after the Revolution. Accustomed to the sea, the Maritime fishermen naturally undertook to carry their fish to their markets and thus "Bluenose" ships first ventured into deep-sea carrying. The markets of the West Indies were many, small and scattered which prompted the Maritime captains to diversify their cargoes to facilitate ready disposal of them. Thus the production of lumber, potatoes and miscellaneous small manufactures was stimulated at home and these articles were added to the cargoes which cleared for the West Indies.

In the same way, the large-scale exploitation of the forest got its first stimulus from the establishment of colonial timber preferences during the wars with Napoleon. A large trade with Great Britain in square timber grew up and reached its peak about 1850. As the stand of large trees suitable for this trade approached exhaustion, a demand arose for lumber, particularly in the United States. Saw-mills sprang up at the mouths of the rivers in the Maritimes and exports of sawn lumber and deals began to replace square timber. In the sixties, the Bay of Fundy lumber trade was one of the chief world staple trades in terms of volume. The carrying of these bulky timber products always made large demands on shipping and the Maritimes were early drawn into building their own wooden ships for the purpose. Most of the rough ships used in this trade were sold in the same market as the timber and lumber which they carried.

The shipbuilding and carrying trades sprang from the basic Maritime occupations but soon grew beyond them. At the middle of the last century, the Maritimes were one of the world's great commercial maritime powers, holding fourth place in registered tonnage of shipping. They had begun by building ships to carry their own produce and this still provided the backbone of the business. In addition, however, the vessels of Nova Scotia and New Brunswick were engaged in the trade from Europe to the United States, to South America, the East Indies and Australia. They carried coal from England to the East, guano from the Chincha Islands to England and France, petroleum from the Gulf ports to Europe and South America and wool from Australia to Europe. The "Bluenose" vessels were to be seen in every great port in the world.

The principal industries of the Maritime colonies were thus closely allied and in large measure

complementary. It was impossible to think of the lumber or fishing industries apart from the shipbuilding and carrying trades and, on the other hand, anything which threatened the carrying trade would compel fundamental and sweeping readjustments in the other occupations. It was a highly unified and integrated economy. In a personal and more intimate sense, several of these occupations were often unified in a single enterprise carried on by one individual or trading group.⁸

Thus the Maritimes had mastered the techniques of the wood-wind-water era. On the basis of forest products and fish, they had made a place for themselves in world industry and trade. All their minor and subsidiary occupations were nicely geared to support and develop these leading industries. This balance in their economy and the perfection of their skills signified a confident maturity which enabled them to compete on even terms in the deep-sea carrying trade.

Nova Scotia was the most diversified of the Maritime Provinces. Its exports were of a greater variety and spread over a wider range of markets. Nevertheless, in 1866, fish accounted for over 40 per cent of the value of total exports.⁹ The trade in fish was almost entirely with the West Indies and the United States, the former outlet in 1866 being only slightly more important than the latter. The Reciprocity Treaty, which gave free entrance to the American market, and the Civil War had greatly stimulated the fishing industry in Nova Scotia. Between 1860 and 1866, the value of Nova Scotia fish exports rose by almost one-half and about three-quarters of this increase was absorbed by the expanding market in the United States.

It is difficult to state precisely the relative importance of the principal occupations since so many worked in several industries at the same time. The schooners employed in fishing in the spring participated in the West Indies trade during the fall and winter. Most of the fishermen combined farming and lumbering with their fishing. A highly individualistic and resourceful people used their farming operations to establish a marked

degree of self-sufficiency while they secured supplementary cash income from fishing and lumbering. A great many of them were, at one time or another, engaged in the carrying trade. In addition to those who made it a part-time employment, the carrying trade provided full-time occupation for about 13 per cent of the gainfully employed in Nova Scotia in 1866.

Nova Scotia built her ships for her own purposes rather than for export. In the period between 1863 and 1866, the annual value of ships built was as much as one-third of the total value of all exports. The vessels owned by Nova Scotians in 1865 represented an investment of about \$9 million compared with a total capital investment in manufacturing of \$6 million. The available statistics do not suffice to give a distinct and complete picture but they do indicate that the life of Nova Scotia was dominated by the sea.

The economy of New Brunswick had a much simpler pattern than that of Nova Scotia. It was virtually a vast lumber camp. In 1866, forest products (excluding ships) made up nearly 70 per cent of the total exports of New Brunswick. Apart from subsistence fishing and farming, lumbering with its allied shipbuilding and carrying trade made up practically the entire economy. Great saw-mills were located chiefly at the mouths of the St. John and the Miramichi Rivers giving employment to three or four thousand men while half as many again were occupied in the logging activities which fed the mills. Thousands of farmers derived a substantial part of their income from logging and from growing hay, oats and potatoes for the lumber camps.

The ships built to carry the lumber to foreign markets were the most specialized product of the New Brunswick economy. Between 1862 and 1865 the value of ships built in New Brunswick varied from three-quarters to one-half of the value of all other exports.¹⁰ Shipbuilding thus had a major place in the economy. It was the one manufacturing activity (aside from the simple processing of the saw-mill) in which the Province had a differential advantage, providing an alternative to mere extraction and export of raw materials. Most of the towns were greatly dependent on the employment it offered. It brought in a relatively large amount of income from abroad as about half the output of ships was exported. The carrying trade was not nearly as important as it was in Nova

⁸ The following account brings this out clearly. "The lumber for these assorted cargoes came from small local mills. Many of these mills would be owned and managed by men who had farms in the neighbourhood and whose interests also extended to the sea and ships. The Bluenose farmer, proclaimed the handiest man in the world, was commonly credited with raising the potatoes for his cargo, felling and sawing the lumber for it, building his own schooner in his spare moments and finally sailing her down to the Islands where he turned merchant and disposed of his wares." A. R. M. Lower, *The North American Assault on the Canadian Forest*, p. 70.

⁹ Minerals made up 16 per cent of all exports, forest products 11 per cent, agricultural products about 20 per cent, and a miscellaneous group of products, including all manufactures, accounted for only about 12 per cent.

¹⁰ They easily exceeded by one-third the value of ships built in Nova Scotia during the same period.

Scotia,¹¹ yet about seven per cent of the gainfully occupied inhabitants of the Province obtained full-time employment in it. The lumbering, ship-building and shipping industries of both provinces, but particularly of New Brunswick, prospered on the demands of the American Civil War. With the coming of peace, the American markets declined sharply.

Prince Edward Island was neatly integrated in this Maritime economy. Its people had retired largely from the sea and taken up farming.¹² It had already become a highly developed and specialized agricultural community. In 1867, it had approximately the same population, number of farms, occupied acreage and grain production as at present.¹³ Its considerable agricultural surpluses went mainly to supply the exporting industries of the neighbouring colonies. These, however, were not adequate to the needs of Nova Scotia and New Brunswick which imported large quantities of food-stuffs annually from the United States.¹⁴

The Last Phase of the "Golden Age" of the Maritimes—the coming of the steamship and the railway

The very substantial prosperity of the three Maritime Provinces in the pre-Confederation years rested upon their fish and lumber exports, wooden shipbuilding and their carrying trade. The maintenance of this "Golden Age", as it has since come to be known, depended on the continued stability and prosperity of each one of this set of closely allied and related industries. By the middle sixties, there were plenty of indications that it rested on a precarious base. The best as well as the most accessible of the timber resources had been cut off. The commercial privileges contained in the colonial preferences and the navigation laws were gone. The provinces had to face the competition of New England in the fish markets of the West Indies, and with the abrogation of the Reciprocity Treaty in 1866, they were compelled to forgo (temporarily, as it turned out) their free market for fish in the United States. The Civil War had stimulated exports and provided new opportunities for the carrying trade. It brought a lush, though temporary

prosperity and masked, for the time being, the long-term factors which were operating against the Maritimes. Once the War was over, the full weight of these factors began to be felt and the "Golden Age" soon became a memory.

It was the coming of the steamship which most surely foreshadowed the decline of this balanced economy of the Maritimes. By 1860, the holds of steamers already supplied about ten per cent of the ocean tonnage of the world and sailing vessels were being forced into longer and less profitable hauls. Steamships were regularly making better Atlantic passages than the fastest sailing ships. The age of steel and steam was ousting the wooden sailing ships and undermining the foundations of the economy of the Maritime Provinces.

The implications of steel and steam were as yet only vaguely realized. Scaremongers might forecast their significance but, as in most human affairs, only a demonstration would carry conviction. The opportunities arising out of the Civil War had carried Maritime prosperity to its highest peak and it was not realized that the assurances given by this bustling activity were superficial, or even false. The Maritime people believed in the sea. They were confident of their power to make any necessary adjustments and maintain their enviable position in the commerce of the world.

If they were not alert to the threat of the steamship, they were becoming very much alive to the promise of the railways. It was seen that railways would improve their communications and open up their own hinterland for development. Many were confident that railways would open markets for coal, fish, and manufactures in the Canadas and draw the expanding commerce of the interior to their seaports. The coal interests of Cape Breton, for example, were strong supporters of the Confederation scheme. For almost the first time, the Maritimes began to feel the pull of the continent behind them.

For upwards of twenty years before Confederation, they had tried to secure the building of a railway to connect Canada with the Maritime winter ports. But projects for the Intercolonial had always collapsed. It was not attractive to private capital. The governments in the colonies were never able to agree on the terms on which it should be built as a joint project. The British Government, whose guidance and assistance alone could have surmounted these obstacles, wanted a military and strategic road, hugging the east shore of New Brunswick, while New Brunswick, in particular, disdained a railway which failed to

¹¹ In the sixties, New Brunswick had only about half the registered tonnage of Nova Scotia.

¹² There was some fishing and at times an important ship-building industry, but farming was by that time by far the most important occupation.

¹³ In the present century there has been a considerable shift toward the production of agricultural specialties such as dairy products, potatoes, cattle and horses.

¹⁴ A large proportion of these imports from the United States consisted of wheat and flour, transhipped from Upper Canada, via Portland.

connect Saint John and Fredericton with the Canadas.

An equally ambitious scheme which failed of fruition was the "European & North American Railway", designed to connect Halifax and Saint John with Portland, Boston and New York and to deliver trans-Atlantic passengers, mail and express freight in record time. The hopes of an imperial guarantee were disappointed and New Brunswick and Nova Scotia could not finance either line themselves. They did, however, build pieces of railways, designed to fit into the larger schemes but insufficient to give them the external connections they desired. Thus by the time of Confederation, the two Provinces had built 379 miles of railway which improved their internal communications but harmed their own coasting trade. The most impressive result obtained was the addition of some \$10½ million to their public debt.

On the eve of Confederation, then, the Maritimes had a mature and prosperous economy, dependent on a wood-wind-water technique fast becoming obsolete. They were beginning to feel the pressures of the revolution in transportation. Their tentative efforts to apply the new technique of steel and steam and to integrate their economies with those of the United States and the St. Lawrence Valley had been unsuccessful, and they were debating the question whether the promise of an intercolonial railway was worth the obligations and the risks of political union with Canada.

*The Canadas—their concern with transportation
—common and conflicting interests*

Upper and Lower Canada, although divided by cultural and sectional cleavages, had never been intended by nature to form separate economic systems. The St. Lawrence, with its access to the sea and its ingress to the continent, was bound to unify its drainage basin economically. There are, therefore, better reasons than the political union of 1841 for discussing the pre-Confederation Canada as an economic entity.

The St. Lawrence basin contained a considerable area of fertile land lying south of the Laurentian plateau. This available land had been largely filled with settlers in the years before Confederation. Along with this rapid agricultural development had come a flourishing pioneer industry, laying the foundations for a diversified economy of modest yet substantial proportions. Under the conditions of the time, it was naturally becoming a community of settlements, devoted to internal

trade and commercial intercourse with the United States.

At the same time, there was an aggressive and ambitious commercial group in Montreal, supported in the later part of the period by the growing commercial interest in Upper Canada, which thought of the St. Lawrence as primarily a trade route and which had vigorously endeavoured to have the whole political and economic structure accommodated to that conception. From the days of the fur trade, the commercial group in Canada had seen the St. Lawrence as an integral part of the old British commercial system and had striven to make the trade of a continent flow through their hands instead of through New York. Successive colonial governments had been inspired by this dream with the result that government policy and public finance had been harnessed to the grandiose conception of the St. Lawrence as a trade route. In ambitious but always futile efforts to realize this great plan, the Province had accumulated a set of public works and a crushing public debt, both too massive for an economy limited by its own boundaries.

New York had challenged the St. Lawrence trade route, first by the Erie Canal and then by the railways. Canada had countered, first, by the canal system of the St. Lawrence, built as a government project, and second, by the Grand Trunk Railway, undertaken by private capital but relying heavily on government loans. Both Canadian ventures failed to attract the trade of the American Middle West. In 1862, soon after the completion of the route, the Grand Trunk Railway Company was in serious financial difficulty.

The Government of Canada had gambled heavily in railway development through the fifties and early sixties. By 1866, it had loaned \$33 million to railway companies while municipalities had contributed \$7 million. Virtually the whole of the \$40 million, which made up forty per cent of the total provincial and municipal debt, was uncollectible. If canals are included, the government investments in transportation amounted to almost sixty per cent of the provincial and municipal debt. Altogether, about one-third of the current expenditures of the Province and the municipalities were incurred on transportation. The attempt at commercial integration with the interior of the continent had irretrievably failed and left behind it a burden of debt which weighed oppressively on the economy.

The railway development of the preceding decade had opened up the country for settlement and for exploitation of its great timber resources remote from the river valleys. The flow of immigrants had filled up the most promising parts of the Province and almost all the good agricultural land had been occupied. By 1866, forty-one out of the fifty-one million acres surveyed had been disposed of. The pioneer type of community must expand outwards and the substantial limits of that type of expansion in the Province had been reached.

Despite the concentration of public expenditures on the development of the trade route, agriculture had become the most important source of livelihood in Ontario and Quebec and it had displaced the forest as the chief source of exports. The latter, however, retained much of its old importance. Lumber had succeeded fur as the great staple emerging from the St. Lawrence. The industry prospered, first, on the British colonial preference and then on the expanding markets of the United States. Farming communities grew up around and depended on it. The coming of the railways increased the available supplies and general expansion and the American Civil War stimulated demand. The building of wooden ships flourished at and near Quebec and the lumber trade made this city one of the great shipping centres of the world at the time.¹⁵

Over half of those gainfully occupied in the Province of Canada were employed in farming and lumbering. In the period, 1860-65, agricultural and forest products provided over four-fifths of the exports. The combined stimulus of the Reciprocity Treaty and the Civil War had greatly increased the exports of both groups of commodities to the United States.¹⁶ The abrogation of the Treaty threatened very serious consequences, particularly for agriculture the exports of which were almost double those of the forest industry during the period 1860-65.

The Rise of Manufacturing in the Canadas

The manufacturing industry had grown rapidly and was becoming diversified after 1850. The new industrial methods spreading out from England were attracted by local supplies of raw materials and the natural shelter arising from lack of transportation facilities. The revenue tariff afforded some incidental protection. Under such

circumstances, local production of some articles was more economical. Accordingly, most of the manufacturing industry was scattered in small units through the towns and villages of the agricultural settlements. Generally, it was of a kind which required little capital and little highly specialized skill. As the railways spread, there was a tendency toward increase in size of unit and concentration in strategic centres. There had long been a large flour-milling industry in Montreal, catering to the export trade, and industries began to concentrate in Hamilton and Toronto. In general, however, manufacturing enterprise remained small, simple and decentralized. Almost every town produced agricultural implements and the other tools used by a pioneer community. Machinery and tools requiring a high degree of skill for their production were almost entirely imported. Woollen mills, boot and shoe factories, furniture factories, breweries and distilleries thrived on local raw materials and the incidental protection of a revenue tariff. But in such commodities as cotton and linen textiles, dependent on foreign raw materials, no progress was made toward local production.

In spite of the rapid development, the total industrial factory production was small. This was by no means entirely due to the economic advantage of buying cheap foreign manufactures with exports of raw materials. To a degree which we now find hard to realize, individual households were self-sufficient. There was also a large group of craftsmen who lived largely by barter. The blacksmith, carpenter, shoemaker, tailor and dressmaker produced a variety of the basic necessities, often in return for produce or a share of the raw materials used. In the census of 1871, this group of craftsmen reported an output equal to one-fifth of the total of all manufacturing establishments, excluding saw mills and flour mills.

Cheap and improved transportation had already begun to draw industry from the farm and the village to the city. But the huge concentration of industry into large units in the relatively few great industrial centres of today had to await further developments in transportation, the improvement of old and the invention of new techniques, the extension of markets and the perfection of the joint stock company as an instrument for collecting large pools of capital. At the time of Confederation, small enterprise still ruled the field. In 1870, the average capital invested per establishment was \$1,900 compared with \$217,000 for 1930. In 1870, the three leading urban centres contributed about

¹⁵ Almost half the population of the City of Quebec was directly supported by the shipbuilding industry alone.

¹⁶ Total exports to the United States, which had averaged scarcely \$9 million for the period 1852-54, had grown to an average of about \$19 million for the period 1860-65.

one-quarter of the total net value of manufactures while today they contribute nearly one-half. In 1867, there were not more than 50,000 labourers employed in all the cities of the four provinces.

Self-Sufficiency—the importance of the family as an economic and social unit

Seventy or eighty years ago, material income was, for most, limited to the basic requirements of food, clothing and shelter. These were chiefly the product of local industries, geared to local consumption, and in which individual enterprise was predominant. To a great extent, they were secured without passing through the money exchange system at all. Thus the sharp and frequent trade fluctuations of the period did not cause profound dislocations. The simplicity and decentralization of factory industry and the ease with which the worker could retreat to the self-sufficient farm gave to the economy a capacity for adjustment which it has largely lost in later years with the shift to large-scale organization and urban concentration.

In Lower Canada, agriculture was on a more nearly self-sufficient basis than in any of the other provinces. Very little was produced for sale and the farmer was absorbed in the manifold activities necessary to make the family a self-sufficient economic unit. In Upper Canada, on the other hand, newer soil and larger holdings yielded considerable surpluses for sale. The surpluses in the early days were mainly wheat; and relentless cropping provided large exports in the days of the colonial wheat preference, and later during the Crimean War. In the sixties, decline in fertility of the soil, the Reciprocity Treaty and the American Civil War resulted in a greater diversity of products. By 1866, exports such as barley, rye and cattle had become important. Exports of cheese were still small and the sale abroad of commodities such as tobacco, fruits and vegetables had to await improvements in transportation and the development of a more intensive and specialized agriculture. Although agricultural exports increased greatly in the decade before Confederation, the return from this market provided a relatively small part of total farm income, the average income per farm from this source being from sixty to seventy-five dollars per year.

The increase in cash income and the high prices for many products during the American Civil War were coaxing many farmers away from self-sufficiency and into specialization. This movement, however, was just beginning and the farm

household in Upper Canada was still a basically self-sufficient unit. Food was grown and processed at home. The raw products of the farm were turned into articles of wear with the assistance of the local shoemaker and tailor who would take produce in return for their services. Such necessities as tea, sugar, hardware and certain articles of clothing which could not be produced at home were generally obtained by barter from the local general store. Tallow was turned into candles, fatty refuse into soap, and the tools which were beyond the ingenuity of the farm workshop could generally be contrived by the local blacksmith.

What was true of the Upper Canada farm was even more true of the agricultural communities in Lower Canada and the Maritimes¹⁷, where such things as furniture, carts, and carriages were frequently made on the farm. The farm of the period was a miniature factory or combination of factories. Much of the work of the large industrial army of today, concentrated in highly specialized factories in the cities and towns was, in that early period, performed in a multitude of rural households.

However prices might fall and cash income from other sources might melt away, the farm household always produced enough to prevent abject poverty. This fact had its importance for other industries as well. The farm was often a base of operations, on which individuals could fall back when other projects and occupations ended in disaster. In the Maritimes, agriculture, fishing and lumbering were closely allied. Everywhere the family and its relatives were a close economic unit; the various members helped one another when new enterprises were started or old ones failed. The material basis for this mutual welfare association was the family farm.

The Economic Outlook of the British North American Colonies—the coincidence of unfavourable developments

The closely inter-related activities of the Maritimes dependent upon the wood-wind-water techniques, and the agricultural, forestry and commercial economy of the Canadas had achieved a considerable prosperity in the decade before Confederation.

¹⁷ In 1870, seven and a half million yards of woollen cloth were produced on farms in Canada. This was nearly equal to the total value of the output of the numerous woollen mills and the imports of woollen cloth combined. In a speech at Halifax in 1865, A. G. Archibald referred with pride to the Maritime agriculturalists: "the great body of settlers in the country whose backs are covered with woollens of their own production, whose feet are shod with the hides of their own cattle, who sleep between blankets of their own wool and their own weaving—on feathers from their own farmyards." *Evening Express*, January 4, 1865.

However, in each of the British North American colonies the basis of that prosperity threatened to disappear as the 1860's drew to a close. The Province of Canada had a transportation system which had been conceived for a continental commerce rather than for its own needs as an economic unit. The commercial dream had evaporated and left a paralyzing burden of public debt. Further industrial expansion depended on expanding markets. Unfortunately, the limits of great agricultural expansion had been reached. The best land was occupied and profitable exploitation of the poorer land depended upon buoyant foreign markets for agricultural exports. The outlook for such export demand was gloomy. Hopes for renewal of the British preferences had been extinguished. Most threatening of all was the loss of American markets for agricultural products, foreshadowed by abrogation of the Reciprocity Treaty and the agricultural expansion of the Middle Western States. For five months of the year, Canada had no outlet to the sea and there was constant fear that the United States would make good its threat to withdraw the bonding privileges for Canadian trade. The factors which had made for expansion in the past had practically played themselves out.

The full significance of this is clearly revealed by the movements of population. From 1851-61, the British North American colonies are estimated to have held the equivalent of their own natural increase and a net balance of 175,000 immigrants over emigrants. From 1861 to 1871, there was a net emigration of over a quarter of a million, involving the loss of about one-third of the estimated natural increase for the period.¹⁸ Canada was failing to attract immigrants and losing her native sons. The prospects indicated decline rather than expansion. And on a declining rather than an expanding prosperity the burden of the large public debt would become intolerable.

The economic outlook compelled the Province of Canada to search for a means of escape from hampering burdens and limitations. Judging from the spectacular progress of the United States, the coming of railways had made practicable the hitherto vague project of acquiring Rupert's Land and of linking up with the colony on the Pacific. They would also furnish winter access to the sea through the Maritimes. By bringing this area,

stretching from sea to sea, under a single government, vast new possibilities for expansion would be opened. The trade of the Orient would be tapped and a great internal market, integrating the occupations and resources of all the colonies, would be established. With some reorganization, the transportation system of the Province of Canada could be transformed into an important link of a national transcontinental system. It would cease to be a burden and become a valuable asset which Canada could contribute to the joint capital needed for the new venture. It is significant that the Grand Trunk Railway Company, whose fortunes were as much at stake as those of the people of Canada, reached the same conclusion. The president of the company, Edward Watkin, came to Canada in 1862 to investigate its difficulties. He decided that the only hope of salvage was the launching of a larger venture and thenceforth he was a powerful and effective advocate of union of the British North American colonies.

The opening up of the Northwest had had a romantic appeal in the eastern colonies for two decades. Its possibilities were imagined to be great, but there was little on which to base an estimate of its solid possibilities. The Red River Settlement contained scarcely ten thousand people. Most of these were half-breeds. The manner of their livelihood had been fixed by the activities of the Hudson's Bay Company and they were indifferent to any intensive cultivation of the soil. However, the isolation of the Settlement was over. Hundreds of carts were employed in overland transport between Fort Garry and St. Paul. There were steamboats on the Red River and American settlers and railways were pushing toward the ill-defined lands of the Company. The new methods of transportation were threatening the Hudson Bay route and disposing the governors of the Company to consider the future closely. Inside the settlement, the settlers were dissatisfied with the Company Council's rule.

Beyond the mountain barrier, on the Pacific Coast, the two colonies of Vancouver Island and British Columbia were united in 1866. Union had been brought about largely by the staggering public debt and repeated budget deficits. These colonies had just experienced a mushroom growth, due almost entirely to the gold rush which began in 1855 and which collapsed suddenly about ten years later. In the first year of the gold boom, it is estimated that some 25,000 people entered the two colonies. The feverish search for gold produced a rapid but precarious expansion. Trade and con-

¹⁸ These figures are for all the provinces. But the Province of Canada had three-quarters of the total population and there was little movement of population in the Maritimes, particularly in the latter decade. The figures, therefore, give a substantially correct picture for the Province of Canada.

struction flourished and the subsidiary industries of lumbering and agriculture sprang up. The Government piled up large debts in promoting developments such as the Cariboo road. Then suddenly the rich gold diggings petered out and population fell sharply. In 1866, the total immigrant population of the new Province of British Columbia was little more than ten thousand. The credit system built up to serve the new mining enterprises crashed and buoyant optimism was replaced by gloom and depression. The public debt mounted to more than one hundred dollars per white inhabitant and the budget could not be balanced. British Columbia, depressed and discontented, was concerned to extricate itself from isolation and the burden of the public debt.

Union—a common means of escape and renewed expansion

Thus, for diverse reasons, the economic outlook of all the British North American colonies on the eve of Confederation had many alarming and depressing features. It was a significant coincidence that all the colonies, travelling their separate and well-nigh independent paths, reached an economic cross-roads at the same time. The Canadas, burdened with the failure of their two great bids for western expansion, and dispirited by the closing of their own frontier, were in need of a new outlet and stimulus. The Maritimes, tied to a dying industry, were in even greater, if less conscious, need. The tiny Red River Settlement was beginning to find its feet, but was toddling into the arms of the United States in the process. The Pacific Coast gold rush had fostered some basically sound development, but its recessions had left a small population stranded with a large debt.

Isolated as were the colonies from one another, the Maritime colonies and the colony of Canada were brought together by certain common characteristics in their external relations and the effects of technological changes on their economies. All had been deeply affected by the radical change in imperial commercial policy; all had turned hopefully to the United States and had established profitable but precarious relations; all were deeply alarmed at the prospect that these might be rudely terminated. The impact of the steamship, the railway and the industrial revolution had affected them all profoundly, if variously. The new means of transportation made possible a union of continental proportions in which all hoped to find escape from existing difficulties and stimulus for renewed expansion and prosperity.

3. THE NATURE OF CONFEDERATION

Principal Objectives

Confederation was conceived as the solution for a number of political and economic difficulties and, therefore, had both political and economic aims. Politically, it was designed to establish a new nation to meet the changed conditions of British policy and to brace the scattered provinces against possible American aggression. Economically, it was intended to foster a national economy which would relieve dependence upon a few industries and lessen exposure to the effects of the economic policies pursued by the United States and Great Britain.

Political union was expected to promote strength as against the external world. The triumphant Northern States appeared a threat to territorial integrity. Other interests needed protection too. Nova Scotia felt her deep-sea fishery interests threatened, and the special institutions and culture of Lower Canada would not long have survived absorption of the colonies by the United States. Political union was designed to defend navigation rights on the St. Lawrence and its canals, and fishing rights at sea. A single united authority could use both these and access to its extended internal market as bargaining counters for advantages in international trade. A stable political authority would restore the public credit, so badly damaged by the accumulation of debt and political dissension. In the money markets of the world, the credit of the whole would be greater than that of the parts and would provide a broader base for the government expenditures necessary to attain new and difficult economic objectives.

Federal union was a plan whereby, through mutual concession, cultural and local loyalties could be preserved and reconciled with the political strength and solidarity of the whole. These separate loyalties were strong and their existence was keenly realized. They existed not only in Canada but also in the Maritimes where they had helped to frustrate projects for Maritime legislative union. Mutual concession required the English-speaking elements of Lower Canada to relinquish their integral union with the English-speaking people of Upper Canada while the French-speaking Canadians abandoned their objections to a superior political authority in whose councils they would be in a minority. In compensation, the broad questions of trade and commerce which so intimately concerned the English-speaking people of Lower Canada were to be given to the federal

authority, thus securing the benefits of single control in these matters of general interest while French-speaking Canada was to be secured in sole control of the cherished values it so tenaciously held. Equally, this solution offered security for the historic traditions firmly rooted in the Maritimes.

Economically, the first objectives of Confederation were to establish a free-trade area comprising the five old provinces and to develop inter-provincial transportation facilities. The resources and industries of the several provinces, it was thought, would prove complementary to each other, and would increase prosperity and self-sufficiency. To make this a reality, the Inter-colonial Railway was to link the Maritime Provinces with the St. Lawrence Valley and to give Canada winter access to the sea.

Another great economic objective of Confederation, to be realized as soon as circumstances permitted, was the opening up of the Northwest and the inclusion of the Pacific province. For the Province of Canada, in particular, this westward expansion was to provide an escape from a *cul-de-sac* and the threatened economic stagnation. New frontiers and new resources would provide opportunities for settlement and development. It was recognized as an immense undertaking for which no specific detailed plan could be made under the urgencies and limitations of the moment.

This project had to await the acquisition of the lands of the Hudson's Bay Company. It required the building of a transcontinental railway. This, in turn, depended upon attracting new capital and capital, at that time, had become shy of Canadian ventures. Collective effort and resources on a scale which only government could secure were necessary and, at the same time, conditional on the restoration of the public credit.

Although these plans were necessarily vague in 1867, they were nevertheless resolutely held. The new political framework was designed to give the Federal Government ample powers for the prodigious task of opening up the West. The Federal Government was intended to give a vigorous lead in the development of the new national transcontinental economy and in matters relating to that development there was to be no doubt, such as had recently arisen in the United States, about its authority.

There were some among the Fathers of Confederation who favoured a unitary state as an instrument for realizing these plans. As is well known, John A. Macdonald had a strong preference for a unitary state and Galt accepted the

federal scheme with reluctance and hoped it might later coalesce into a legislative union.¹⁹ But legislative union was not acceptable to the French-speaking Canadians or to the Maritime Provinces. Furthermore, municipal institutions had not yet been established in the Maritimes, and they were still in the early stages of development in Lower Canada. The centralization of all governmental powers under one government was, therefore, impracticable from an administrative point of view. The distractions of local administration might well have diverted some of the energies of the central government from its larger creative tasks. Thus, for various reasons, the builders of the new nation planned a federation comprised of a central government with authority over matters of general and common interest and provincial governments with authority over matters of local concern.

The Division of Legislative Powers

The British North America Act was the final embodiment of their scheme. The acknowledged necessity of a federal type of union was recognized by the preamble to the Act which recited the desire of the Provinces of Canada, Nova Scotia and New Brunswick "to be federally united into One Dominion". The vital core of a federal constitution is the division of legislative powers between the central authority and the component states or provinces. This division represents the compromise between the forces which make union possible and those which inhibit the formation of a closer union. It marks the limits of what can be done by common agreement and the extent to which the separate states must be permitted to differ and work out their own destinies. In sections 91 to 95 of the British North America Act, the main lines of this division were set forth.

In section 92, certain classes of subjects were enumerated and the provinces were given exclusive power to make laws in relation to matters coming within these classes of subjects. These classes included such things as the administration of justice, municipal institutions, the establishment and maintenance of prisons, hospitals, asylums and charitable institutions and control over the public lands of the province. The provinces were also given control over local works and undertakings. But an exception reserved international and inter-provincial lines of transport and communication to the Dominion and authorized the Dominion to take legislative power over any local work at any time

¹⁹ *Speech on the Proposed Union of the British North American Provinces*, delivered at Sherbrooke on Nov. 23, 1864, p. 22.

by declaring it to be for the general advantage of Canada or for the advantage of two or more provinces. A power of direct taxation to raise revenue for provincial purposes was given, although it was thought that expanding revenues from the public lands would make it generally unnecessary for the provinces to exercise this power.²⁰

The classes of subjects in section 92 included two of vague and general reference, viz., "Property and Civil Rights in the Province" and "Generally all Matters of a merely local or private Nature in the Province". Section 93 gave the provinces control over education, subject to certain clauses designed to protect the rights of Roman Catholic and Protestant religious minorities. By section 95, the Dominion and the provinces were given concurrent powers over agriculture and immigration, federal legislation to prevail in case of conflict.

The opening paragraph of section 91 gave the Dominion power "to make Laws for the Peace, Order and good Government of Canada, in relation to all Matters not coming within the Classes of Subjects by this Act assigned exclusively to the Legislatures of the Provinces". That is to say, the residue of powers not expressly given to the provinces was reserved to the Dominion. The section then proceeded with a specific enumeration of twenty-nine classes of subjects, illustrating but not restricting the scope of the general words used earlier in the section.

This enumeration included such classes of subjects as defence, criminal law, naturalization and aliens, and the postal system. It also included regulation of trade and commerce, fisheries, banking, currency and coinage, commercial paper, weights and measures, bankruptcy and insolvency and certain other topics of primarily economic reference. It also gave the Dominion unlimited powers of taxation. The concluding paragraph of section 91 provided against these enumerated topics being "deemed to come within the Class of Matters of a local or private Nature comprised in the Enumeration of the Classes of Subjects" assigned to the provinces by section 92. An exception to section 92 gave the Dominion control over all interprovincial and international transportation and communications.

The Problem of Interpreting the Division of Legislative Powers

No amount of care in phrasing the division of powers in a federal scheme will prevent difficulty when the division comes to be applied to the

variety and complexity of social relationships. The different aspects of life in a society are not insulated from one another in such a way as to make possible a mechanical application of the division of powers. There is nothing in human affairs which corresponds to the neat logical divisions found in the constitution. Therefore, attempts to exercise the powers allotted by the constitution frequently raise questions as to its meaning in relation to particular circumstances.

The British North America Act has not escaped this difficulty. Manifestly, it would be difficult for the Dominion to make any law for the "Peace, Order and good Government of Canada" without affecting, in some way, one or other of the specific subjects in relation to which the provinces were given exclusive powers. On the other hand, laws made by the provinces under the heads of jurisdiction given by section 92 would frequently have direct implications for the "Peace, Order and good Government of Canada" or would bear in some unexpected way upon the enumerated classes of subjects in section 91 over which the Dominion was given exclusive power. The implications and sometimes the express provisions of legislation would seem to cross the line which, in theory, divided the spheres of legislation assigned to the provinces and the Dominion. In a variety of circumstances, the problem of what amounted to an invasion of the field of one by the other would raise difficult questions of interpretation.

The task of interpretation was complicated by the existence, in sections 91 and 92, of several general descriptions of the ambit of legislative power given to the Dominion and the provinces which lacked a clear, legal meaning. "Peace, Order and good Government", "Regulation of Trade and Commerce", "Property and Civil Rights in the Province" do not convey precise signification. Since 1867, the Privy Council has had the last word on the meaning of the British North America Act and has laid down rules of construction for determining when section 91 was to have primacy over section 92. By a process of textual criticism, it has given some concreteness to the general phrases just mentioned. In this way, it has elucidated the legal meaning of the constitution and imparted greater certainty to the division of powers than could have existed when the Act first came into operation. This legal meaning is binding on all other courts and on the Dominion and provincial legislatures.

The British North America Act was a statute of the British Parliament and the Privy Council

²⁰ Speech by Galt, *Confederation Debates*, p. 88.

brought to its task of elucidation an elaborate set of rules binding on the courts in their interpretation of all statutes. These rules required the Privy Council to consider the literal meaning of the words used without any conjectures as to the intentions of those who framed the Quebec and London Resolutions. The Privy Council as a court was not free to consider historical evidence about intentions but was bound to restrict itself to a consideration of what may be called, by contrast, legal evidence—the intention actually expressed by the words used in the Act.²¹ Much controversy, past and present, has centred on the question whether the intention which the Privy Council has found to be expressed in the Act accords with the actual intention of the Fathers; in short, whether we now have the constitution which they intended to give us.

Some are satisfied that the Privy Council has merely made explicit what the Fathers intended. Others dismiss the controversy on the ground that we cannot now know what they intended. Others, again, hold that the constitution today is vastly different from what its framers meant it to be and seek to support their contentions from certain historical evidence. The interpretation given by the Privy Council will be considered in later chapters. In an account of the forces behind Confederation and of the nature of the constitution established in 1867, it is important to note the historical arguments which form the basis of many current criticisms of the Privy Council.²² For purposes of record, we summarize these arguments here but, as we shall indicate later, we do not accept them as conclusive upon certain points, some of them of considerable importance. The critics of the Privy Council do not appear to have fully substantiated their case but, at the same time, they do marshal an impressive mass of historical evidence in support of their general conclusions and their arguments cannot be dismissed as mere hypotheses. Confederation being relatively close to us in time, and the records of its achievement being relatively ample, it is argued we have no reason to assume that it is inherently impossible to determine now the intentions of the Fathers, although it may well be admitted that it is difficult to establish with conclusive finality the meaning of

some of the phrases which they employed. The historical case presented by the critics of the Privy Council has not been accepted by all authorities but it merits the attention and consideration of serious students of the problem.

Historical Interpretation of the Intentions of the Fathers—arguments supporting a broad view of Dominion powers

Some historians urge that the Fathers intended to give wide, sweeping powers to the Dominion and to restrict the provinces to a narrow range of functions, in the exercise of which they were to be subject to the control and supervision of the Dominion.²⁴ They claim that the general phrases in section 91, "Peace, Order and good Government" and "Regulation of Trade and Commerce", to which the Privy Council has given a restricted meaning were intended to have a broad interpretation and that the general phrase, "Property and Civil Rights in the Province", in section 92, to which the Privy Council has given an extended meaning, was intended by the framers to have a much more limited interpretation.

Some of the leading figures among the framers of the federal scheme evidently intended the general government, as it was called, to have broad and far-reaching powers. John A. Macdonald explained that "all the great questions which affect the general interests of the Confederacy as a whole, are confided to the Federal Parliament".²⁵ Galt declared that among the subjects given to the general government would be found "all that could in any way be considered of a public and general character".²⁶ Lord Carnarvon, the Colonial Secretary, introducing the scheme to the House of Lords said it proposed to give to the central authority "those high functions and almost sovereign powers by which general principles and uniformity of legislation may be secured in those questions that are of common import to all the provinces".²⁷

²⁴ For historical interpretations in general supporting this view, see Appendix D, G. Creighton, *British North America: Confederation*; R. G. Trotter, *Canadian Federation* (Toronto, 1934); "The Coming of Confederation," *Cambridge History of the British Empire*, Vol. VI, pp. 438-62; Chester Martin, "British Policy in Canadian Federation," *Canadian Historical Review*, Vol. XIII, pp. 3-19; W. M. Whitelaw, *The Maritimes and Canada before Confederation*, (Toronto, 1934); W. P. M. Kennedy, *Essays in Constitutional Law*, p. 85ff; V. C. Macdonald, "Judicial Interpretation of the Canadian Constitution," *University of Toronto Law Journal*, Vol. I, No. 2, p. 260ff. For careful description of the Quebec Conference see W. M. Whitelaw, "Reconstructing the Quebec Conference," *Canadian Historical Review*, Vol. XIX, pp. 123-37.

²⁵ *Confederation Debates*, p. 40. See also pp. 30, 33, 41.

²⁶ *Speech on the Proposed Union*, p. 10.

²⁷ Quoted by V. C. Macdonald, "Judicial Interpretations of the Canadian Constitution" (1936), *University of Toronto Law Journal*, p. 263.

²¹ In interpreting the British North America Act, "the question is not what may be supposed to have been intended but what has been said." Lord Sankey in *Edwards v. Attorney General of Canada*, [1930] A.C. 124 at p. 137.

²² E.g., C. H. Cahan, *The British North America Act, 1867*, an address delivered before the Canadian Club of Toronto, September 15, 1937; cf. *Report pursuant to Resolution of the Senate to the Honourable the Speaker, by the Parliamentary Council relating to the Enactment of the British North America Act*, Ottawa, 1939.

Some of the opponents of the scheme criticized it on much the same grounds. A. A. Dorion claimed that it "gives all the powers to the Central Government, and reserves for the local governments the smallest possible amount of freedom of action,"²⁸ and J. B. E. Dorion opposed the scheme "because we are offered local parliaments which will be simply nonentities, with a mere semblance of power on questions of minor importance".²⁹

Supporters of this historical interpretation urge that this view of the relative importance of the Dominion and provincial governments in the new scheme is borne out by various sections of the constitution. They point to the power of the Dominion to appoint the Lieutenant-Governors of the provinces and emphasize the fact that while the provinces were given power to amend the provincial constitutions, they were forbidden to alter in any way the office of Lieutenant-Governor. They contend that the intention to give the Dominion a dominating position is confirmed by the power to reserve and disallow provincial legislation which was given to the Dominion.

In support of this general position, they place great importance on the opening paragraph of section 91 which gave the Dominion power to make laws for the "Peace, Order and good Government of Canada" in relation to all matters not exclusively assigned to the provincial legislatures. This phrase had acquired a wide, though not very precise, significance in the legislative history of the British Empire before 1867.³⁰ "Peace, order and good government", and the variation, "peace, welfare and good government" were the phrases habitually used by the British colonial authorities in vesting colonial legislatures with the full range of their legislative powers.

In conferring these powers on colonial legislatures, it was not customary to enumerate specific powers; it was customary merely to grant, in one or other of these well-worn phrases, the entire measure of jurisdiction deemed compatible with imperial control. As imperial control in the internal affairs of the colonies was mainly exercised through the power of disallowance, these phrases carried complete internal legislative competence. In fact, they are the title-deeds of the legislatures of the self-governing Dominions, not again added to by imperial legislation until the Statute of Westminster. The exponents of this historical interpretation, emphasizing the breadth

of Dominion powers, infer from the insertion of this phrase in section 91, that the framers must have intended its full historic meaning to prevail, saving only the powers expressly given to the provinces in section 92.

It is similarly urged that the Fathers meant an extended signification to be given to the phrase "Regulation of Trade and Commerce", in section 91. At the time of Confederation, Canada was just beginning to emerge from the commercial into the industrial age. The distinguishing feature of the commercial age was its pre-occupation with exchange, the trading of raw or crudely processed products on a world-wide scale. This required an extended organization, interprovincial and international in its scope. It was a delicate system, for its life-lines were everywhere exposed. Prosperity depended on its maintenance and its maintenance and development, in turn, depended on the sympathetic consideration, if not the positive assistance, of governments. Nothing showed this more clearly than the British imperial trading organization of the 18th and early 19th centuries. British North American statesmen had lived with this system and had seen what control over extended trading relationships by a single government could achieve. Trade and commerce, because of their nature and scope, were inevitably public matters of great import and it is argued that the phrase "the regulation of trade and commerce" had a very wide significance both historically and in the current usage of the Confederation period.*

In addition, it is contended, they must have been acutely aware of the confusion which arises when control over such matters is parcelled out among several governments. During the fifty years in which the Provinces of Upper and Lower Canada maintained their separate existence, the control of the St. Lawrence and its commerce had been divided between two distinct and independent governments. This division led to conflicts between Upper and Lower Canada and to bitter struggles between the commercial and agrarian parties in each.³¹ Upper Canada had disagreed with Lower Canada and the commercial interests in Montreal had quarrelled with the leaders of the Patriot party over many economic matters of common concern to the whole St. Lawrence Valley.

The impossibility of arriving quickly at a vigorous common policy in these matters had hampered Canada in its bid for the trade of the mid-continent.

²⁸ *Confederation Debates*, p. 250.

²⁹ *Ibid.*, p. 859.

³⁰ C. H. Cahan, *op. cit.*

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* Appendix 2—D. G. Creighton, *British North America at Confederation*, pp. 53-4.

³¹ These conflicts are examined in detail in D. G. Creighton, *The Commercial Empire of the St. Lawrence, 1760-1859*.

The frustrations engendered by divided authority formed part of the living memory of public men at the time of Confederation and this appeal to history for a broad interpretation of Dominion powers argues that the Fathers, who wanted to create a robust national economy, must have intended the control of such matters to be placed in the hands of a single government.

In support of this thesis, they draw attention to the reluctance among the commercial element in Montreal to give up the Union of 1841 which had established a common government to deal with these economic matters. The confederation plan asked them to abandon this union and one of the tasks of the advocates of a wider union was to convince them that the establishment again of two provinces in the St. Lawrence Valley would not mean a return to the old confusions. John Rose assured them that they had nothing to fear because the general legislature would have control over the post office, trade, commerce, navigation:—"all the great and important interests . . . that affect the minority in Lower Canada . . .".³² Galt reiterated that "the interests of trade and commerce . . . would be taken out of the category of local questions . . .".³³ Cartier, stating that he could understand the concern of the commercial minority of Lower Canada lest there should be a return of the old difficulties, said these fears were groundless because "it would be for the General Government to deal with our commercial matters".³⁴ On the basis of these statements, supporters of this historical interpretation argue that the words "Regulation of Trade and Commerce", were intended to transfer a wide range of economic matters to the control of the central authority.³⁵

A historical interpretation which would magnify the scope of Dominion powers by attaching a limited special meaning to the phrase, "Property and Civil Rights in the Province" has also been urged. This phrase has had a long history in British North America, rising out of the relationships of French and English in the valley of the St. Lawrence. British statesmanship sought a solution of this racial problem which would preserve to French Canada the institutions which were vital to its way of life. The Quebec Act of 1774 secured "His Majesty's Canadian subjects within the Province of Quebec" in the enjoyment of their property and civil rights and provided

that "in all matters of controversy relative to property and civil rights, resort shall be had to the laws of Canada as the rule for the decision of the same".

In the constitutional and legislative enactments of both Upper and Lower Canada, there were a number of references to the law "relating to property and civil rights". In these references, the phrase was used to signify either the common law of England or the French customary law. That is to say, it denoted the set of laws and customs which were at once the expression and support of the distinctive ways of life of the French-speaking and English-speaking Canadians. The phrase found its way into sections 92 and 94 of the British North America Act.

Supporters of a broad view of federal power argue that the sole purpose of introducing the phrase "Property and Civil Rights in the Province" into section 92 was to protect the unique institutions and ways of life of the Province of Quebec. They lay strong emphasis on section 94 which contemplates certain conditions under which the federal authority may secure unrestricted power to make uniform laws "relative to Property and Civil Rights in Ontario, Nova Scotia and New Brunswick". To them, this section suggests that the phrase had reference only to matters on which these three provinces were in fundamental agreement and that regional differences of interest were not involved. Ontario, Nova Scotia and New Brunswick, with their acceptance of the English common law, were in agreement on precisely those matters in which each differed so completely from Quebec. Thus it is argued that the inclusion of this phrase in section 92 was not designed to express genuinely local as against national interests nor to fix the spheres of the different levels of government but rather to protect regional interests only in so far as they were specifically cultural in character.

This historical interpretation, therefore, maintains that the phrase, "Property and Civil Rights in the Province", as used in section 92, was intended to cover only what was necessary for this limited but important purpose of safeguarding the cultural autonomy of Quebec. It appeals to statements of British officials prior to the passing of the Quebec Act of 1774 and to the instructions of the British Government to the Governors of Quebec after 1774 as showing what were long understood to be the essential laws for safeguarding the fundamental institutions and ways of life of Quebec. These instructions to the Governors repeatedly

³² *Confederation Debates*, p. 409.

³³ *Speech on the Proposed Union*, p. 20.

³⁴ *Confederation Debates*, p. 61.

³⁵ See Appendix 2—D. G. Creighton, *British North America at Confederation*, pp. 50-52.

commanded that the Canadians were to enjoy the "benefit and use of their own Laws, Usages and Customs in all Controversies respecting Titles of Land, and the Tenure, Descent . . . of Real Estates, and the distribution of the personal property of Persons dying intestate . . ." ³⁶ Accordingly, the phrase in question would include matters of civil law concerning the relations of citizen and citizen, such as ownership, transfer and various dealings in property, inheritance and succession by will, rights arising from personal status, such as minority and capacity to make contracts, and from the intimate domestic relations of the family. It would include a variety of other matters of private law but it would not include a number of matters inextricably bound up with the public law such as nation-wide regulation of industry and trade. Still less could it include social insurance which had formed no part of either French or English law and the idea of which was unknown to those who framed the British North America Act. In this way, it is sought to infer from historical evidence an intention to give the phrase "Property and Civil Rights in the Province" a much more restricted meaning than that given to it by the Privy Council.

Historical Interpretation of the Intentions of the Fathers—arguments supporting a broad view of provincial powers

These historical arguments as to the intentions of the Fathers of Confederation and the meaning assigned by them to general phrases such as "Peace, Order and good Government", "Regulation of Trade and Commerce" and "Property and Civil Rights in the Province" have not gone without challenge on historical grounds.³⁷ For example, it is urged that the expression "property and civil rights" has always had a very wide meaning in our constitutional history.

By Royal Edict in 1663, Louis XIV of France created a Sovereign Council at Quebec giving it the power "de connaître de toutes causes civiles et criminelles, pour juger souverainement et en dernier ressort selon les lois et ordonnances de notre royaume",³⁸ thus, it is claimed, establishing in Quebec the entire French law which ruled New France at the time of the conquest.

The Royal Proclamation of George III of England in October, 1763, which proposed to introduce the English common law into the conquered territory in North America was naturally resented as a grave injustice by the people of Quebec. The Quebec Act of 1774 which was passed to meet this grievance, repealed the proclamation of October, 1763. Section 8 of the Act declared that "His Majesty's Canadian Subjects, within the province of Quebec . . . may also hold and enjoy their Property and Possessions, together with all Customs and Usages relative thereto, and all other their Civil Rights, in as large, ample, and beneficial Manner, as if the said Proclamation . . . had not been made" and then continued to provide, as quoted above, that the laws of Canada should provide the rule of decision in controversies "relative to Property and Civil Rights". This section of the Quebec Act has never been repealed.

The French law in its entirety was in force in New France at the time of the conquest and the people of Quebec desired to retain it. This was the ground of their objection to the Proclamation of 1763 and the Quebec Act was passed to meet this grievance. On the basis of these facts, it is argued that the Quebec Act was intended to meet the grievance fully and that the expression, "Property and Civil Rights", as used in the Act, was intended to comprise the entire French civil law and not merely certain selected portions of it. The only thing which is important for understanding the scope of the Act is the purpose for which it was passed. The statements of British officials and the instructions of the British Government to colonial governors merely reveal their opinions. They do not give clues to the meaning of phrases used in the Quebec Act.

This argument attributes a very wide meaning to the expression "Property and Civil Rights" as used in the Quebec Act, and holds that when used in later statutes, the expression bears the same extended meaning unless an express limitation is introduced. No express limitation on the meaning of the phrase occurs in the British North America Act and therefore it is concluded that the broad meaning given to it by the Privy Council is in accordance with its original historical meaning.⁴¹

³⁶ W. P. M. Kennedy, *Statutes, Treaties and Documents*, p. 156.
³⁷ P. B. Mignault (formerly Mr. Justice Mignault of the Supreme Court of Canada), "Nos Problèmes Constitutionnels" (1928), 16 *Revue du Droit*, p. 577; V. Evan Gray, "The O'Connor Report on the British North America Act" (1938), 17 *Canadian Bar Review*, 309.

³⁸ "to deal with all civil and criminal cases, to judge finally and in the last resort according to the laws and ordinances of our kingdom".

⁴¹ For this argument, see P. B. Mignault, *op. cit.*

The Limitations of the Historical Arguments

All the historical interpretations go far afield for their arguments. There is no final certainty as to what the framers meant by the use of these phrases. The records of the time have not preserved all their opinions on all points. Clear statements of the views of some on particular points have come down to us; of the views of others, nothing is known.⁴²

All that is certainly known is that the framers had large plans for the new Dominion and they proposed a strong central government with ample financial powers to carry the program through. The financial settlement which gave the Dominion the unrestricted taxing power, and the exclusive use of the most important revenue sources of the time (nearly four-fifths of the former provincial revenues were given to the new Dominion Government) is the most significant evidence of the leading role cast for the new Federal Government and of the responsibilities which it was expected to assume. In the provisions for reservation and disallowance of provincial legislation, the Fathers gave the Dominion legal power to supervise and control the legislatures of the provinces. At the same time, it was agreed that the state should be federal with exclusive spheres of power reserved to both the provinces and the Dominion. But the exact meanings intended to be given to the general words used in outlining these exclusive spheres of legislative power remain a matter for speculation.

There is no doubt that some of the framers had wanted a legislative union. Those who expected to be members of the new Federal Government naturally wanted a large stage on which to exhibit their capacity as statesmen.⁴³ But whatever their intentions, they could not overcome the limitations imposed by physical conditions. They could not ignore the social forces rooted in the history of the colonies any more than they could presume to bind the future indefinitely to the past.

There is a further limitation inherent in all historical interpretation of political constitutions which are to govern the distant future. The framers of the constitution could not foresee the

revolutionary economic and social changes that have since taken place and therefore could have no intention at all concerning them. Whatever powers Confederation was intended to confer on the Dominion, these intentions cannot provide answers for many of the questions which agitate us now for the simple reason that the conditions out of which present difficulties arise were not even remotely considered as possibilities. The intentions of the founders cannot, except by chance, provide solutions for problems of which they never dreamed.

4. PUBLIC FINANCE AT CONFEDERATION

The Sphere of Government in 1867

The character of a public finance system depends on what governments are expected to do. What governments are expected to do depends on the prevalent political opinion and stage of development of the economy of the time. The statesmen of Confederation did not anticipate any radical change in the functions of government, but the adoption of a federal union required an allocation of responsibilities and sources of revenue between the Dominion and the provinces. In making a financial settlement and in fixing the future financial relationships of the provinces with the new Federal Government, they assumed that the sphere of governmental action would remain essentially what it had been in the past. Therefore, they were primarily concerned to transfer to the Federal Government the responsibilities and the financial resources which would enable it to carry out the political and economic objectives of the union.

Since 1867, there have been sweeping economic and social changes and no less important changes in opinion as to the appropriate functions of government, none of which could have been anticipated at the time. It is necessary to recall the social conditions of the day and the limited scope of government activities in order to appreciate the financial arrangements with which the federation was equipped and to realize that the division of responsibilities and revenue sources which was made at Confederation contemplated a much smaller sphere of government activities than exists today. The manner of life in British North America has already been briefly outlined. It will suffice to recall here the scattered rural character of the population, the decentralization of industry in small towns and villages, the self-sufficiency of families and communities, the impressive solidarity of the family, and the open frontier

⁴²The agreement reached by delegates to the Quebec Conference is acknowledged to have been a compromise and it is unlikely that the delegates, in the subsequent discussions, always distinguished clearly between the compromise and their own conception of what Confederation should have been. For a clear statement of the difficulties attending historical interpretation, see V. Ewan Gray, "The O'Connor Report on the British North America Act", (1933), 17 *Canadian Bar Review*, 309 at pp. 315-8.

⁴³John A. Macdonald probably had the possibility of a great future in mind when he said, "We are all mere petty provincial politicians at present; perhaps by and by some of us will rise to the level of national statesmen." Quoted by A. R. M. Lower in "Sir John A. Macdonald", (1939), 19 *Dalhousie Review*, p. 86.

of the continent which afforded individuals a variety of means of adjustment to economic crises. While economic conditions did not offer great material prosperity to the many, they provided a modest security for the frugal and industrious and an almost frictionless adjustment to business fluctuations without any intervention by governments.

The role which governments were called upon to play was one peculiar to the conditions of the time. An individualistic outlook, which relies on the family as the unit of mutual welfare, is nourished in a pioneer society and people readily agree that governmental action should be confined to the narrowest possible limits.⁴⁵ Accordingly, the principal functions of the state followed the prescription of Adam Smith. Government was thought to have met its purpose when it provided for adequate defence, the enforcement of the general law through the equal administration of justice and the maintenance of a few essential public works. Within this framework of order provided by public authority, individuals were expected to work out their own destiny unrestrained and unassisted by governments. There was a general conviction, widely confirmed by contemporary example, that Providence helps those who help themselves.

British North American governments did not concern themselves with regulation of the daily pursuits of the people. Nor did they assume any significant responsibility for social welfare. They took seriously their responsibilities for maintaining defence and internal order but they carried them out with frugal care. Thus far their interpretation of the doctrine of *laissez faire* was in harmony with current British precept and example.

But the application of the doctrine was modified by certain conditions peculiar to the colonies. The United States and all European countries at the time had incurred huge burdens for defence. European governments were spending as much as half of their current revenues on military purposes, and the United States had just emerged from a costly civil war. The colonies, relying on Great Britain, escaped most of the costs of military and

naval defence. Had they been able to stop at this point, their burden of public expenditures would have been extremely low. However, release from expenditures on defence gave them resources for other tasks and all the colonies took on heavy commitments in aiding economic development.

Pioneer communities in North America were always hampered in realizing their dreams of progress by the tremendous difficulties of transport and communications. The scarcity of capital and the scattered nature of settlement added to the difficulties. As a result, the task of securing the provision of community equipment such as canals, harbours, roads, bridges and railways was saddled on government. Of all the agencies of the community, it had the broadest command of means. Until this equipment was provided, development was slow and individuals could not reap the rich promise of a new country. The colonial interpretation of *laissez faire* did not forbid strenuous government activity for developmental purposes.⁴⁶ The state was required, by general consensus, to help people to help themselves.

*The Burden of Debts incurred for Development—
the necessity for centralization of finance*

The urgent demand for transportation facilities had played havoc with the otherwise careful public finances of the colonies. In particular, the Province of Canada had gambled heavily in developing the St. Lawrence route as a means of tapping the trade of the Middle West. The coming of the railways, with their fabulous promise, intensified this concentration of public finance on development. Canada put in another expensive bid for commercial greatness by extensive railway loans. The Maritimes were stirred to link themselves to the continent behind them and the governments undertook ambitious railway programs as public works. By the eve of Confederation, transportation had overshadowed everything else in the budgets of the colonies and had seriously strained the public finance systems of Canada, New Brunswick and Nova Scotia.

⁴⁵ In the sixties of the last century, the philosophy of *laissez faire* was at the height of its influence upon public policy throughout the world.

⁴⁶ Appendix 2—D. G. Creighton, *British North America at Confederation*, pp. 67-70.

TABLE 2.—DEBTS OF THE B.N.A. PROVINCES ON THE EVE OF CONFEDERATION^(a)

(Millions of Dollars)

	Canada June 30, 1867	New Brunswick June 30, 1867	Nova Scotia June 30, 1867	Prince Edward Island June 30, 1873	British Columbia Dec. 31, 1869	Total
Gross Debt.....	79.8	7.9	9.3	4.1	1.5	102.6
Less Cash, Marketable Investments, Sinking Funds, etc.....	5.4	0.1	0.3	0.2	0.4	6.4
Net Debt.....	74.4	7.8	9.0	3.9	1.1 ^(c)	96.2
Net Debt accounted for as follows:						
Railways—Direct Investments and Loans.....	33.3 ^(d)	4.5	6.3	1.2	—	45.3
Commitments re construction of Railways.....	—	1.9	1.0	2.0	—	4.9
Canals.....	18.7	—	—	—	—	18.7
Sub-total.....	52.0	6.4	7.3	3.2	—	68.9
Loans and Investments on which partial or no Interest was paid.....	14.7	0.2	—	—	—	14.9
Other Public Works.....	9.8	^(e)	^(e)	^(e)	—	9.8
Other Commitments.....	13.0	—	—	—	—	13.0
Deficit or Surplus (+).....	15.1+	1.2	1.7	0.7	—	11.5+
Sub-total.....	22.4	1.4	1.7	0.7	1.1 ^(c)	27.3
Total Net Debt.....	74.4	7.8	9.0	3.9	1.1 ^(c)	96.2

^(a) Compiled from the Public Accounts of the B.N.A. Provinces.^(b) In the Maritime Provinces, roads, bridges, lighthouses, harbour improvements and other public works were charged to current account.^(c) Approximate.^(d) Including unpaid interest of \$13.1 million.

Fully three-fourths of the total debt of the British North American Provinces had been incurred for transportation.⁴⁷ Most of it had been piled up rapidly after 1850 and while it was represented by much new and valuable community equipment, it was not directly productive from the point of view of public finance. The Canadian canals had failed dismally as an attempt to tap the Middle West and most of the Canadian railways were in financial trouble soon after they were completed. The Government of Canada had assisted them with large loans which quickly fell into default.⁴⁸ In the Maritimes, practically the entire provincial debts had been incurred on

publicly-owned railways, the interest charges on which had to be met by the governments out of general taxation. In 1866, the service of the provincial debt absorbed 21 per cent of the current revenues of Nova Scotia, 28 per cent of those of New Brunswick and 30 per cent of those of Canada.

These dead-weight debts, which had accumulated so rapidly, seriously endangered the credit of the provinces in the London money market. They resulted in repeated budget deficits and it became increasingly difficult to secure loans at rates the provinces could hope to bear. Deficits had driven home the necessity for the union of Vancouver Island with the mainland and the infant Province of British Columbia was struggling with a public debt which amounted to over \$100 per white inhabitant.⁴⁹ The situation was only less severe in the other provinces. They were being obliged to fall back on temporary loans from local banks and from English banking houses.⁵⁰ All the

⁴⁷ Of the Province of Canada's net debt of \$74 million, over \$18 million had gone into the canal system and \$33 million into loans to railways. In addition, the Province had shouldered municipal obligations (which, with arrears of interest, amounted to \$14 million) arising mainly out of rash municipal support of railway development. The Maritime Provinces had a direct investment in publicly owned railways of \$11 million. With the exception of a small amount in Nova Scotia, the capital commitments of the Maritime Governments consisted exclusively of obligations contracted for roads and railways.

⁴⁸ \$13 million out of the total loans to railways of \$33 million consisted of unpaid interest.

⁴⁹ Howay, *British Columbia, The Making of a Province*, p. 163.

⁵⁰ In 1866, Canada was paying 8 per cent interest on one of these temporary advances.

provincial governments had overplayed their roles of promoting development.⁵¹ They were seriously embarrassed in carrying their existing obligations and their separate public finance systems could not hope to undertake new burdens. Yet there was a powerful demand for new and greater developmental projects. These could not be achieved without the centralization of finance.

Public Expenditures before Confederation—the importance of development

The restricted role of governments and the nature of public functions in the society of British North America are most clearly demonstrated by the magnitude and distribution of the government expenditures. The figures are relatively insignificant when compared with those of today. In 1866 less than one-twentieth of the income of the

population flowed through government channels and the total public expenditures amounted to less than \$6 per capita.⁵² The major factor in this striking contrast with the present time was the relative unimportance of the cost of education and public welfare; less than 14 per cent of the total expenditures were devoted to these services in 1866. The elemental responsibilities of government (i.e., the administration of justice, legislation and general administration), were conducted with frugality. The cost of defence which had been assumed by the Imperial authorities left no heavy burden on the colonies. All the traditional functions of government absorbed less than 40 per cent of the total outlay. The remainder of the expenditures (including debt charges), which comprised nearly one-half of the total were devoted to development. This purpose dominated the public finance of the provinces.

TABLE 3.—EXPENDITURES ON CURRENT ACCOUNT—FISCAL YEARS ENDED 1866^(a)
(Thousands of Dollars)

	Province of Canada		Nova Scotia		New Brunswick		Total
	Provincial	Municipal ^(a)	Provincial	Municipal ^(a)	Provincial	Municipal ^(a)	
<i>Development:</i>							
Net Debt Charges ^(a)	3,214	1,400	306	40	349	50	5,359
Transportation, including roads and bridges.....	952	950 ^(a)	490	20 ^(a)	213	25 ^(a)	2,650
Public Domain and Agriculture.....	256	—	85	—	16	—	357
Sub-total.....	4,422	2,350	881	60	578	75	8,360
<i>Traditional Functions:</i>							
Justice, legislation and general government.....	3,235	1,850	351	65	217	60	5,778
National Defence.....	1,641	—	145	—	151	—	1,937
Sub-total.....	4,876	1,850	496	65	368	60	7,715
<i>Welfare and Education:</i>							
Public Welfare.....	340	300	101	10	44	10	805
Education.....	583	900	156	25	116	30	1,820
Sub-total.....	923	1,200	257	45	160	40	2,625
Miscellaneous.....	350	—	36	—	58	—	444
Total.....	10,571	5,400	1,670	170	1,164	175	19,150

^(a) Compiled from the Public Accounts of the B.N.A. Provinces.

^(b) Estimates based on Municipal Returns for Upper and Lower Canada, *Seasonal Papers* (1867-8) No. 7.

^(c) Estimated.

^(d) Gross interest charges less interest received.

^(e) Excluding value of statute labour.

⁽¹⁾ This was not true of Prince Edward Island in 1866, but by 1873, that Province had also incurred paralyzing debts in aid of railway construction.

⁽²⁾ In 1937, total government expenditures in Canada amounted to \$90 per capita and were equal to one-fourth of the national income.

There were no marked differences in the total government expenditures of the three provinces. The current expenditures of the provincial governments in the Maritime Provinces on roads, education and public welfare were significantly higher than those of Canada. This was mainly due to the fact, that in the Maritimes, municipal institutions did not exist outside the principal cities and public expenditures on roads and bridges, education and public welfare became items in the current expenditures of the provincial governments. On the other hand, the existence of more fully developed municipal institutions in Canada, particularly in Upper Canada, upon which a great part of the burden of maintaining roads and supporting education and public welfare had been placed, resulted in a corresponding reduction of provincial expenditures on these items.

The Maritime Provinces relied almost entirely on a simple customs tariff of a revenue nature and made practically no attempt to levy excise at all.⁵³ As Table 4 indicates, each of them derived 80 per cent or more of its revenues from this source in 1866. The taxation system in Canada was somewhat more advanced. In 1866, customs duties provided 66 per cent of the provincial revenue while 17 per cent was derived from excise. With a more diversified economy, Canada did not import so wide a range of articles of general consumption. Local production had developed in many lines and there were considerable elements of protection in a tariff which ranged around 20 per cent on articles of general consumption.

In both Canada and the Maritimes, the customs rates were considerably higher on luxury items.

TABLE 4.—REVENUE—CURRENT ACCOUNT—FISCAL YEARS ENDED 1866^(a)
(Thousands of Dollars)

	Province of Canada		Nova Scotia		New Brunswick		Total
	Provincial	Municipal ^(b)	Provincial	Municipal ^(c)	Provincial	Municipal ^(c)	
Taxes:							
Customs.....	7,328	—	1,226	—	1,037	—	9,591
Excise.....	1,889	—	6	—	—	—	1,895
Realty.....	—	3,800	—	120	—	125	4,045
Other.....	107	700	—	10	—	10	827
Sub-total.....	9,324	4,500	1,232	130	1,037	135	16,358
Licences, Permits, Fees, etc.....	281	500	7	30	9	30	857
Public Domain.....	903	—	129	—	108	—	1,140
Sales of Commodities and Services.....	509	—	84	—	93	—	686
All Other.....	35	400	18	10	7	10	480
Total.....	11,052	5,400	1,470	170	1,254	175	19,521

^(a) Compiled from the Public Accounts of the B.N.A. Provinces.

^(b) Estimates based on Municipal Returns for Upper and Lower Canada, *Sessional Papers* (1867-8) No. 7.

^(c) Estimated.

The Principal Sources of Public Revenue—the dependence upon customs duties

The revenue systems of the three provinces were markedly similar and chiefly notable for their simplicity. The provinces relied almost entirely on indirect taxation with scarcely any effort to impose direct taxation. They did not have any elaborate tax machinery for the nature of the economy and its modes of distributing income made it useless to attempt a more complex system of taxation. Hence their principal revenues were derived from customs duties and excise which lent themselves easily to assessment, collection and enforcement.

However, the simple, frugal society of the time did not consume any great quantity of the heavily taxed luxuries and the gradations of the tariff rates did not provide any significant measure of progressive taxation. The duties on articles of general consumption produced the great bulk of the revenues of the provincial governments. Table 5 shows the per capita burden of the principal taxes in the three provinces and reveals the complete dependence on these indirect taxes.

⁵³ The import duties on commodities of general consumption ranged around 10 per cent in Nova Scotia and 15 per cent in New Brunswick.

TABLE 5.—PER CAPITA CURRENT REVENUES,
FISCAL YEARS ENDED 1866
(Dollars)

	Province of Canada		Nova Scotia		New Brunswick	
	Pro- vincial	Muni- cipal	Prov- vincial	Muni- cipal	Pro- vincial	Muni- cipal
Customs.....	2.77	—	3.37	—	2.53	—
Excise.....	0.71	—	0.02	—	—	—
Realty.....	—	1.44	—	0.33	—	0.46
Licences, Permits, Fees, etc.	0.11	0.10	0.02	0.08	0.03	0.11
Public Domain.....	0.34	—	0.35	—	0.40	—
All Other.....	0.25	0.41	0.28	0.06	0.37	0.07
Total.....	4.17	2.04	4.04	0.47	4.63	0.64
Combined Provinces and Municipalities.	6.21		4.51		5.27	

Except for two or three leading cities, municipal organization was virtually non-existent in the Maritimes. Thus the income from import duties carried the burden of practically all local expenditures as well. In Canada East, municipal development was well under way but it was still considerably behind that of Canada West. In the Province of Canada the revenues of the fully organized municipal system were nearly equal to half the total revenues of the provincial government. Municipal institutions had enabled the provincial government to transfer very substantial responsibilities from its own shoulders without materially cutting down its own sources of revenue. Thus Canada could face the difficult and rather unpredictable adjustments of a major change with more equanimity than could the Maritimes.

This was the public finance structure which the architects of Confederation had to remodel to suit their new purposes. It included large debts incurred almost entirely for public works such as canals, harbours and railways as well as heavy current expenditures for developmental purposes. The traditional functions of government absorbed a substantial part of the revenues but only very modest sums were allotted to education and public

welfare. Apart from the direct taxes levied by the municipalities of Canada, these various burdens were almost entirely supported by indirect taxation consisting of customs duties and excise. These debts and functions of government and these sources of revenue were now to be allotted between the provinces and the new Dominion.

*The Division of Responsibilities and Revenues
under the British North America Act*

The new financial settlement was in part determined by the legacy of debts and the character of the economy. It was guided by the prevailing philosophy of the functions of government and the fiscal experience of the past. But within these conditions, the actual shape of the revised system of public finance was dictated by the purposes which the new political structure was designed to serve. In the future, the Federal Government was to provide for defence and have jurisdiction over interprovincial communications. It was required to build the Intercolonial railway; expected to deepen and improve the canal system of the St. Lawrence; pledged to open up communication with the West; in short, it was to take the major responsibility for national security and national development. The transfer of these costly functions would greatly reduce the burdens on the provincial governments.

Because the Dominion was to assume the responsibility for development, the massive community equipment and assets of the provinces, which could be adapted to its purpose, were to come under Dominion control and it was to assume the debts which the provinces had incurred in acquiring them. Harbours, lighthouses, steamboats, canals and railways were to be brought within its jurisdiction and where owned by the provinces, to become the common property of the Dominion. With minor exceptions, the public debts of the provinces were completely assumed by the Dominion. This is indicated in detail in Table 5A on the following page.

TABLE 5A.—PROVINCIAL ASSETS AND LIABILITIES ASSUMED BY DOMINION AT CONFEDERATION
(Thousands of Dollars)

	Province of Canada	New Brunswick	Nova Scotia	Total Assets and Liabilities assumed by Dominion July 1, 1867	British Columbia July 20, 1871	Prince Edward Island July 1, 1873	Total Assets and Liabilities assumed by Dominion
Debt assumed by Dominion:							
Direct Debt.....	60,621	5,146	6,062	70,829	1,168	1,688	73,685
Guaranteed Debt.....	150	—	—	150	—	—	150
Savings Bank Deposits.....	—	777	645	1,422	—	250	1,672
Treasury Notes in Circulation.....	3,114	—	606	3,720	—	—	3,720
Temporary Loans.....	3,097	108	342	3,547	310	—	3,857
Capital Liabilities.....	8,212	1,869 ^(b)	975 ^(c)	11,056	—	2,021 ^(d)	13,077
Current Liabilities.....	21	—	404	425	10	140	575
Trust Funds.....	1,945	—	—	1,945	—	—	1,945
Gross Debt assumed by Dominion.....	76,160	7,900	9,034	93,094	1,488	4,099	98,681
Assets taken by Dominion as Offsets to Debt:							
Cash.....	1,461	20	303	1,784	42	—	1,826
Sinking Funds.....	1,889	—	—	1,889	442	—	2,331
Assets re Guaranteed Debt.....	37	—	—	37	—	—	37
Investments.....	390	87	—	477	—	—	477
Current Assets.....	321	—	—	321	4	—	325
Total Assets taken by Dominion as Offsets to Debt.....	4,098	107	303	4,508	488	—	4,996
Net Debt Assumed by the Dominion.....	72,062^(e)	7,793	8,731	88,586	1,000	4,099	93,685
Debt Allowance as per B.N.A. Act.....	62,560	7,000	8,000	77,560	1,066	4,701	83,867
Assets transferred to Dominion:							
Investments.....	607	—	—	607	—	—	607
Loans, Advances, etc., excluding railways, on which partial or no interest was paid.....	1,150	240	—	1,390	—	—	1,390
Public Works and Loans to Railways:							
Railways—Direct Investments and Loans.....	33,256 ^(a)	4,514	6,123	43,893	—	1,213	45,106
Canals and Harbour Improvements.....	21,296	—	—	21,296	—	—	21,296
Roads and Bridges.....	1,763	—	—	1,763	—	—	1,763
Public Buildings and Miscellaneous Works.....	4,607	—	—	4,607	—	—	4,607
Total Public Works and Loans to Railways.....	60,822	4,514	6,123	71,499	—	1,213	72,712
Current Assets.....	144	—	—	144	—	—	144
Total Assets transferred to Dominion.....	62,763	4,754	6,123	73,640	—	1,213	74,853

^(a) Subsequent adjustments, due largely to capitalisation of annuities, increased the net debt of the Province of Canada to \$73,006,068.84 at June 30, 1872.

^(b) Commitments for subsidies to railways in the course of construction. At June 30, 1868, \$465,764.57 had been paid on this account.

^(c) Light Houses, Harbour Improvements, Roads and Bridges and other public works were transferred to the Dominion but as they were charged originally to current revenue, they do not appear in the statement of assets.

^(d) Except for \$21,437.47 for provincial pensions capitalised, this comprises commitments for subsidies to the Windsor and Annapolis Railway.

^(e) Treasury Notes in circulation on June 30, 1873, amounting to \$37,311.10, were called for cancellation by the Province.

^(f) Balance due on commitments for construction of the Prince Edward Island Railway.

^(g) Loans and unpaid interest, Grand Trunk Railway, Great Western Railway and the Northern Railway. Unpaid interest amounted to \$13,000,000.

Debt allowances, in round sums but calculated roughly on an equal per capita basis, were allotted to all provinces; it was provided that provinces whose actual debt fell below the allowance should receive interest at 5 per cent per annum from the Dominion on the difference, and the provinces whose debts exceeded the debt allowance should pay interest on the excess at the same rate.

The magnitude of the burdens, actual and prospective, which were being transferred to the Dominion, called for commensurate fiscal resources and powers. Therefore, it is not surprising that

many of the Fathers spoke as if all the significant powers of taxation were to be given to the Dominion. At Sherbrooke, Galt declared, as if speaking of an undivided power, that "the power of taxation had been confided to the General Legislature".⁵⁵ Both the Quebec and London Resolutions stated that subsidies were to be paid to the provincial governments "in consideration of the transfer to the General Parliament of the powers of taxation".⁵⁶ Although it was expected at the

⁵⁵ Speech on the Proposed Union, p. 11.

⁵⁶ Quebec Resolutions No. 64; London Resolutions No. 52.

time that the Federal Government would rely upon the accepted and well-tried devices of indirect taxation, such as customs and excise, for raising the necessary revenues, the possibility that unforeseen circumstances might compel it to extend its levies to direct taxation as well persuaded the framers to give the Dominion unlimited powers of taxation.

National security, national development and the fostering of trade and commerce by appropriate regulation were regarded by the Fathers as the great functions of government. They were also the functions which they thought likely to expand in the future. When these had been transferred to the Federal Government, the provinces were left with functions, the burden of which was not expected to grow. They would be required to support a civil government establishment; to maintain a number of local public works and to undertake the administration of justice. But the heaviest duties of civil government and the onerous burden of the great public works would be lifted from their shoulders. The support of education was to come within their sphere and their control over "Generally all Matters of merely local or private Nature in the Province" and over "the Establishment, Maintenance and Management of Hospitals, Asylums, Charities and Eleemosynary Institutions in and for the Province" implied responsibility for social welfare problems which got beyond the resources of charitable and municipal organization.

Of the functions remaining to the provinces, the support of education bulked the largest financially. It took the form of financial assistance and did not require extensive administrative machinery. Moreover, the assistance was of a modest character. The nature of the economy explains the small per capita expenditure on education. In the self-sufficient rural or village society of the time, education in a broad sense was obtained without much benefit of formal schooling. There was a farm and fishing apprenticeship in fact as well as a craft apprenticeship, none of which involved the expenditure of public funds. Schooling was not compulsory. The professions afforded few openings and parents wishing to prepare their children for such opportunities were expected to pay for their education at private schools.⁵⁷ The technical complexity of our society in more recent times, which has revolutionized educational methods and costs lay far ahead and unforeseen.

Provincial payments for public welfare were even smaller than those for education ranging in 1866 from 6 per cent of total current expenditures in Nova Scotia to 3 per cent in Canada, the latter percentage indicating that a considerable share of this burden had been unloaded on the municipalities. In fact, most of the provincial expenditures on public welfare took the form of assistance to municipal institutions and private charities.

New Brunswick alone of the provinces had established a permanent board of public health in 1866. When the cholera epidemic startled Canada into establishing a temporary central board of health in 1849, there was considerable objection to assisting private misfortune out of the general public funds.⁵⁸ This spirit was still dominant in matters relating to public welfare. All provinces were contributing to the care of the insane but the amounts were small. The poor and the disabled, the aged and the orphans, were left to the care of municipal and private organizations, assisted, if at all, by small government grants.

The self-sufficiency and solidarity of the family carried a great deal of this burden of providing social security for the unfortunate. Periodic unemployment generally meant no more than a temporary retreat to the family homestead. There was nothing in the experience of the Fathers to suggest serious defects in this pattern of social security. Indeed, there was a disposition to speak hopefully of a time when private charity would relieve the governments of their existing commitments for public welfare.⁵⁹ Personal responsibility was the ideal of the time and many looked forward to a society where it would be perfectly realized.

The functions which were left to the provinces were important but their cost was not large. The minor financial role which was conceived for the provinces in the federation is emphasized by the frequent equation of them to great municipalities. Galt, in his speech at Sherbrooke declared that the local legislatures would be "municipalities of a larger growth"⁶⁰ and members of the Canadian legislature from Upper Canada frequently spoke of them in the Confederation debates as "local municipal parliaments" and as "large municipal deliberative bodies".⁶¹ Tupper, at the Quebec Conference, said it was proposed "to preserve the Local Governments in the Lower Provinces because

⁵⁷ *Canadian Public Health Journal*, 1926, p. 140.

⁵⁸ *Speech on the Proposed Union*, p. 15.

⁵⁹ *Ibid.*, p. 15.

⁶⁰ Appendix 2—D. G. Creighton, *British North America at Confederation*, p. 82. See also p. 79.

⁵⁷ Some grants were made to colleges but they were insignificant in amount.

we have not municipal institutions".⁶² In the Prince Edward Island Assembly, George Coles complained that "in this House, scarcely anything should be left for us to do, but to legislate dog taxes, and the running at large of swine".⁶³ There was repeated reference to "how insignificant are the matters, agreed . . . to be left to the Local Governments".⁶⁴

The calculations of the amounts required for the operation of the provincial governments after Confederation on which the financial settlement was based show the extent to which functions were to be transferred. Tupper estimated that Nova Scotia, which had had an outlay in 1863 of over a million dollars, would be able to meet her responsibilities after Confederation with \$370,000. Similarly, the New Brunswick delegates to the Quebec Conference undertook to perform the local services for \$353,000 after Confederation, in comparison with an expenditure of \$885,000 in 1863. Canada had spent almost \$11 million in 1863 and the new Provinces of Ontario and Quebec were expected to reduce their annual expenditures to a combined total of something over \$2 million.⁶⁵

The Federal Government was to assume virtually all the provincial debts and the large expanding functions of government. With greatly reduced responsibilities, the provinces could have no need for access to the great sources of revenue of the day. Accordingly, section 92 limited the provinces to direct taxation within the province. The provinces were given the public domain with its incidental revenues and a power to impose a variety of licences and fees. These were the sources from which the provinces were expected to finance their activities. The customs duties and excise taxes which provided the great bulk of the revenues were reserved exclusively to the Federal Government.

⁶² Pope, *Confederation Documents*, p. 85.

⁶³ P.E.I. *Assembly Debates*, 1865, pp. 85-7.

⁶⁴ George Brown, at the Quebec Conference. See Pope, *Confederation Documents*, p. 77.

⁶⁵ The figures for the three provinces are those given by Galt in his Sherbrooke address.

TABLE 6.—PERCENTAGE DISTRIBUTION OF COMBINED PROVINCIAL AND MUNICIPAL REVENUES—FISCAL YEARS ENDED 1866

	Province of Canada	Nova Scotia	New Brunswick	Total
Taxes:				
Customs.....	45	75	72	49
Excise.....	11	—	—	10
Realty.....	23	7	9	21
Other.....	5	1	1	4
Sub-total.....	84	83	82	84
Licences, Permits, Fees, etc.	5	2	2	4
Public Domain.....	5	8	7	6
All Other (a).....	6	7	8	6
Total.....	100	100	100	100

(a) Revenue from post office and from sales of other commodities and services are excluded. These are offset by corresponding expenditures.

Revenues Left to Provinces Fall Short of Requirements—gulf bridged by federal subsidies

The transfer of customs and excise to the Dominion left the provincial governments with less than one-fifth of their former revenues. Modest as were the responsibilities they retained, these revenues fell considerably short of meeting them. They were given the power to levy direct taxes but the discussions of the Confederation period indicate that the provincial governments were not expected to use it.⁶⁶ Direct taxes were extremely unpopular; they had never been levied by the provinces, and, as already pointed out, the nature of the economy made the administration of direct taxation except by municipalities very difficult.

In these circumstances, the Fathers felt obliged to seek other means of meeting the prospective deficits of the provinces. The task was complicated by the fact that the deficiencies were much more serious in some provinces than in others. The relatively mature municipal system in the Province of Canada carried a large share of what would otherwise have been provincial responsibilities. Practically all the municipal revenues were raised by a direct property tax. In 1866, the municipalities of Canada collected nearly a third of the total provincial and municipal revenues. The surrender of customs and excise to the Dominion and the provincial power of direct taxation left this municipal revenue system intact. In the

⁶⁶ "It was expected and intended, and for a full generation it was a fact, that the federal subsidies and revenues of the public domain would provide a sufficient revenue for the provinces." Ex. 297, Brief of Out., p. 15.

Maritimes, on the other hand, municipal development had scarcely begun and public expenditures in the localities were being financed largely out of general taxation—from customs revenues which yielded considerably more per capita than in the Province of Canada and which would be handed over to the Dominion at Confederation.⁶⁸ Thus prospective deficiency of provincial revenues under the settlement varied inversely with the degree of municipal development. While Ontario and Quebec were to retain, between them, almost half of the total provincial-municipal revenues collected in the old Province of Canada,⁶⁹ Nova Scotia and New Brunswick were to retain only about one-fourth.

TABLE 7.—DEFICIENCY OF PROVINCIAL REVENUES AFTER CONFEDERATION AS ESTIMATED BY GALT

	Local Revenues	Local Outlay	Deficit
Canada.....	\$1,297,000	\$2,260,000	\$963,000 or 38 cents per capita
Nova Scotia.....	107,000	667,000	\$560,000 or \$1.70 per capita
New Brunswick....	89,000	424,000	\$335,000 or \$1.33 per capita

In his speech at Sherbrooke, Galt presented estimates of what the expenditures of the provincial governments on their reduced responsibilities would be and of the income to be anticipated from the revenue sources left in their hands. These estimates were based on the financial position of the provinces in 1864 and as they provided the basis of discussion for the subsidy calculations, they are set out in Table 7. They show prospective deficits ranging from \$1.70 per capita in the case of Nova Scotia down to 38 cents per capita for the new Provinces of Ontario and Quebec. The Table shows the extent of the gap which somehow had to be bridged if the main lines of the proposed financial settlement were to be retained intact.

⁶⁸ Thus New Brunswick and Nova Scotia would lose 72 per cent and 75 per cent respectively of their combined provincial-municipal revenues while Canada would lose only 56 per cent. The realty and other miscellaneous taxes collected almost entirely by the municipalities in Canada amounted to nearly a third of the total public revenues (municipal and provincial) in 1866. In the Maritimes, these direct taxes yielded less than 10 per cent of the total revenues. See Table 6. Developed municipal institutions accompanied greater urbanization which was presumably an indication of higher taxable capacity.

⁶⁹ The position of Ontario was considerably better than that of Quebec where municipal development was still in its early stages. It is impossible to disentangle the municipal revenues attributable to the two separate areas of Canada before Confederation and no accurate statement of the relative position of the two new provinces can be made.

There was a strong desire to avoid the device of annual subsidies from the Dominion to the provinces. However, the framers of the settlement refused to give the provinces a concurrent power of indirect taxation lest it be used to establish interprovincial trade barriers and they did not believe it was politically possible to impose direct taxation.⁷⁰ Thus there was no real alternative and subsidies were introduced to bring provincial revenues to a level with minimum estimates of future expenditures.

The Quebec Conference found considerable difficulty in reaching a subsidy formula which would satisfy the demands of equity, and meet the wide variation in the anticipated deficits of the different provinces. The prevailing individualism which enforced representation by population in the political sphere assumed without question that the first principle of equity in the financial settlement was per capita equality. However, a per capita annual payment which would bridge the gap for Nova Scotia or New Brunswick would give Ontario far more additional revenue than appeared necessary. Moreover, it would require total annual subsidies in excess of \$5 million a year. This was too large a deduction from the prospective annual revenues of \$12 million to be collected by the Dominion which was undertaking such great responsibilities. Accordingly there was pressure to reduce the estimates of provincial needs. Nova Scotia, where the greatest deficit was expected, revised its estimate of expenditures to a figure which would require an 80 cents per capita subsidy to bridge the gap. This standard, which brought the total annual subsidies below \$3 million, was adopted as the basis of settlement.

This arrangement was still open to the objection that it gave Ontario more than was necessary while it was a very tight fit for Nova Scotia. New Brunswick, pleading special need, was granted an extra \$63,000 for a period of ten years. The 80 cents per capita subsidy was modestly supplemented in the final settlement by lump sum grants for the support of general government, and the provinces were launched with these subsidies as the solvent for their financial weakness.

Although the financial settlement quickly proved to be intolerable for Nova Scotia—a revision being necessary in 1869—its principal features stood for many years and, with minor modifications, it was applied to new provinces as they joined the Dominion. Its terms were written into the British

⁷⁰ Appendix 2—D. G. Craigton, *British North America at Confederation*, p. 85.

North America Act and the subsidies agreed upon were declared to be "in full Settlement of all future Demands on Canada". If the provinces chose to increase their expenditures materially, it was intended that they should obtain their additional revenues entirely from the revenue sources allotted to them.

Summary—the great responsibilities and the dominant financial position of the Federal Government

The financial settlement underlines the various statements of the Fathers as to the great functions of the new Dominion and relatively minor financial role to be played by the provinces. The important responsibility for national defence was transferred to the Dominion and the provincial treasuries were relieved of the incalculable burdens which it might entail. The largest single item of public expenditure in the colonies had been the promotion of economic development. One of the major purposes of Confederation was to apply still greater energies to this task and to provide still larger financial resources for the purpose. In effect, the Dominion was a great holding company designed to unify the efforts of the colonies in realizing the opportunities of a transcontinental domain. All the provincial assets which could be adapted to that purpose were transferred to the Dominion as were the debts which the provinces had incurred in acquiring them. The burden of the functions left with the provinces was expected, in per capita terms, to grow lighter rather than heavier. In the economic and social conditions of the time, the cost of education and public welfare was not

expected to increase disproportionately to the growth of population. It was anticipated that rapid extension of municipal institutions would carry any additional burdens which these services might involve in the future and would reduce the outlay of provincial governments upon them.

The transfer of the dynamic, expanding functions of government to the Dominion while the provinces retained those which were thought to be static or likely to decline explains the lopsided division of the revenue sources of the time. The Dominion was given an unlimited power of taxation to enable it to meet the growing as well as the unpredictable responsibilities of the State. The provinces were left with but fractions of their former revenues. The power of direct taxation had to be given to the provinces in order that they might confer that power on the municipalities which they were expected to create. But all the circumstances of the day seemed to indicate that direct taxation could not be fruitfully employed by

⁷¹The per capita subsidy was based on the census of 1861. As agreed at Quebec, this basis was not subject to change with rising population. However, at London, a concession was made to Nova Scotia and New Brunswick, allowing a decennial revision in their cases until a population of 400,000 was reached. other than municipal governments. It was expected that any additional revenues which a province might need would be found in the growing receipts from the public domain rather than in direct taxation. Subsidies were introduced to make it barely possible for the provinces to balance their budgets. These subsidies were conceived to be final and, subject to a minor exception,⁷¹ were not intended to grow with the growth of population.

CHAPTER II

THE FIRST THIRTY YEARS

1. THE ECONOMIC AND CONSTITUTIONAL BACKGROUND

The enactment of the British North America Act did not of itself assure that balance between national loyalties and interests and provincial loyalties and interests which an effective federal system requires. The Act merely provided a framework within which such a balance might be established. During the first thirty years, Canada had to search for an equilibrium between these two sets of forces. In the early part of the period, the internal and external influences which brought about Confederation continued to operate and their momentum carried the nation-builders through to the main objectives of the union. The Dominion Government vigorously attempted to bring into being the centralized federalism which it recognized as the intention of the Fathers of Confederation. In the later part of the period, provincial loyalties arose in the new provinces and reasserted themselves in the old. Provincial governments contested the dominance of the Dominion and won a signal victory for "provincial rights". The optimism and buoyancy of the first years fixed men's eyes on the broader horizons. In the continued depression of the later years, the visions faded and Canadians were compelled, in the urgent need for adjustment, to turn to the older and more obvious realities of provincial and local community life. In the tug of these forces, the relative strength of national and provincial sentiment gradually became clear and the working principles of Confederation began to emerge.

Rounding Out the Union—Dominion's aggressive program to build a transcontinental economy; all-Canadian transportation and western settlement

The Fathers of Confederation were the agents of the unifying forces. It was they who had the visions of expansion and they who took the helm of government in 1867. As federal cabinet ministers and lieutenant-governors of provinces, they pressed on without serious challenge to round out the union. The attitude of the United States was still aggressive and no settlement of its serious differences

with Great Britain had been reached. In the face of these alarming circumstances, the Dominion Government was forced prematurely into the race for the West. In 1870, the lands of the Hudson's Bay Company were acquired and the new Province of Manitoba was created. The burden of debt in British Columbia was, by this time, more oppressive than ever and the final collapse of the gold boom made it difficult to hope for or to justify the continued separate existence of the colony. Thus the promise of a railway easily brought British Columbia into Confederation and the Dominion from sea to sea became a reality in 1871.

In the meantime, Prince Edward Island had succumbed to the lure of railway building. In 1863, the public debt of the Province had been little over \$250,000. Ten years later, the total provincial liabilities including the commitments for the construction of the Prince Edward Island Railway were more than \$4 million. This was a paralyzing load and the island province which had resisted persuasion in 1866 now accepted the promise of salvation through the remission of debts and entered the Dominion in 1873.

Economic conditions were favourable to the completion of these political objectives. The new Dominion was launched on a rising tide of world prosperity and the assumption of the debts of the new provinces was no excessive burden to the federal treasury. In Great Britain, economic activity was stimulated by easy money and a booming foreign trade; in the United States, by tremendous railway expansion and post-war reconstruction. Between 1868 and 1874 Canadian exports to Great Britain were doubled and, with growing demand and higher prices, a 30 per cent increase in exports flowed into the United States over the trade barriers which had replaced the Reciprocity Treaty. Larger markets for lumber benefited New Brunswick and the Ottawa Valley. Nova Scotia greatly increased its exports of fish and recovered its markets for coal in the United States. Shipbuilding in the Maritimes approached, in 1874, the high peak attained during the Civil War. Agriculture, the most important industry in Ontario and Quebec, nearly doubled its exports in this period.

In this atmosphere of general expansion and prosperity, the Federal Government undertook without hesitation the territorial rounding out of the Dominion, and the transportation developments which were to promote trade between the separate regions. The Intercolonial was built and the canal system of the St. Lawrence was deepened. Expenditures on public buildings, harbours and wharves were greatly increased. With the entrance of British Columbia into the Union in 1871, the building of the Pacific railway became a definite commitment and by 1873 the Dominion had pledged generous assistance to Sir Hugh Allan and his associates in building the railway over an all-Canadian route.

The decision to build the railway entirely through Canadian territory was of fundamental significance. Before Confederation, the colonies had been faced with two broad alternatives. One was to be drawn into the economic orbit, and probably also into the political system, of the United States. This would have led to integration, in each area according to its particular characteristics, with the common neighbour. The economic development of each region would have been determined by the relationships it managed to establish with the country to the south. On the eve of Confederation, it seemed that the price of such relationships would not be less than political assimilation. This consideration turned the colonies to the other alternative which was to ensure political independence through a union of their own and to seek strength and prosperity by a national economic integration based on an expanding inter-regional trade. The pull to the south was strong. The establishment of an east-west integration would require bold and far-sighted policies of national development.

The first of these policies was to provide east-west channels of trade independent of the United States by building a transcontinental railway wholly over Canadian territory. Such a railway would open the undeveloped lands of the West for settlement and fix the political and economic destiny of the area. But the construction of such a line over empty distances and forbidding mountains could not be undertaken without extensive public assistance. This fact pointed to the second policy which was indeed an essential complement of the first. The public lands of the Northwest were to be used by the Dominion to promote railway expansion and rapid settlement. Land grants would provide the greater part of the public assistance required by the railways. The railways, in turn, would make

the lands valuable and a free homestead system would attract a rush of settlers. The decisions to build an all-Canadian railway and to establish a vigorous Dominion land policy were basic national decisions which, together with the adoption of the protective tariff which was soon to follow, fixed the pattern of subsequent economic development in the Dominion.

The technique of combining railway construction and settlement had already been devised and demonstrated in the United States where Canadians had observed the results with envy. Its main features were railway land grants and the free homestead system. The Dominion assured the application of these to the Canadian frontier by the Manitoba Act of 1870. This statute withheld the public lands from the control of the Province and provided that all "ungranted or waste lands" in the entire Northwest should be "administered by the Government of Canada for the purposes of the Dominion". These purposes were made manifest by the free homestead provisions of the Dominion Lands Act of 1872 and the grant of 50 million acres of western lands to the Pacific railway syndicate in 1873.

By 1873, in the short space of six years, the framework of the new transcontinental economic and political system had been erected. The continued rapid expansion of the United States had given the enterprise an urgency it might otherwise have lacked. The "race to the Pacific" had been won and the vital railway and settlement policies had been launched. These were ambitious policies for a small and scattered people but the nation-builders were undeterred by such reflections. "We must not be dribblers in this matter", said the Minister of Finance in 1869. "The opening up of that territory [the Northwest] must be accomplished in a large and comprehensive way."¹ The charge of dribbling could scarcely be laid against them. In six years the Federal Government had committed itself to capital expenditures of almost \$100 million,² as compared with the total debt of \$93 million accumulated by all the colonies in their century of existence before Confederation. But the Government was confident of the ability of the country to carry this burden with ease once the magic of its policies began to work.³ In the meantime, the rising prosperity of the country made the initiation of these policies immediately

¹ Budget Speech, May 7, 1869, p. 34.

² \$30 million for the Canadian Pacific Railway, \$144 million more for the Intercolonial and Maritime railways, almost \$44 million for canals and \$8 million for miscellaneous works.

³ Budget Speech, April 1, 1873.

possible. Between 1868 and 1874, Dominion revenues nearly doubled, most of the increase coming from customs duties. This buoyant financial condition enabled the new Federal Government to consolidate the union and assume the dominant and aggressive role which the Fathers of Confederation had assigned to it. The greatness of its enterprises caught the imagination and evoked the beginning of a national consciousness.

*The Dominion's Paternalism toward the Provinces
—its claim to dominance*

The Dominion Government not only asserted its leadership in economic development; in its attitude toward the provinces, there was much of the old paternalism which had marked the actions of the Imperial Government in colonial days. It maintained that the Lieutenant-Governor was a Dominion officer whose duty it was to reserve bills according to instructions from the Governor General in Council.⁴ In 1868 Sir John A. Macdonald, as Minister of Justice, declared that the Federal Government would be called upon to consider the propriety of allowance or disallowance of provincial enactments much more frequently than the Imperial Government had done in the recent past.⁵

In accordance with this policy, 51 bills were reserved⁶ and 65 acts disallowed⁷ in the first thirty years and, of these, 39 were reserved and 29 disallowed in the first ten years of assertive Dominion leadership. The federal authority proposed to refuse assent on reserved bills and to disallow legislation on several grounds. Thus, it claimed the substantially judicial function of deciding whether provincial legislation was *ultra vires*. It stood ready to invalidate provincial enactments which it thought unjust or contrary to sound principles of legislation. It was prepared to veto legislation which, according to its view, conflicted with imperial treaties or policies, or with Dominion interests and policy.

It was quite in harmony with this theory of its superior position that the Dominion maintained its sole right to supplement the original financial arrangements of 1867 or to fix the terms of admission of new provinces. In 1869, the Dominion Parliament itself increased the subsidies to Nova

⁴ See *Dominion-Provincial Legislation, 1867-98*, pp. 104-5 per Sir John A. Macdonald in 1873 and pp. 77-8, Report of the Committee of the Privy Council in 1882.

⁵ *Ibid.*, pp. 61-62.

⁶ *Memorandum on the Office of Lieutenant-Governor of a Province*, Department of Justice, Ottawa, 1937, pp. 51-60.

⁷ See *Memorandum on Dominion Power of Disallowance of Provincial Legislation*, Department of Justice, Ottawa, 1937, pp. 62-69.

Scotia. A protest by the Ontario Legislature to the Imperial Government against this unilateral action of the Dominion was of no avail, drawing from the Colonial Secretary a reply that the Dominion Parliament had power to make such adjustments. In 1870 and 1871, Parliament, of its own motion, gave Manitoba and British Columbia a larger representation in its councils than the principle of population would have warranted. Arguments that these modifications were contrary to the constitution and required the consent of the provinces were brushed aside and the request for imperial legislation to validate the large scheme of the Manitoba Act of 1870 was made, in accordance with the proposal of the Opposition, by joint address of both Houses of Parliament without consulting the provinces.

However, the forces which made this Dominion leadership and predominance possible waned rapidly after 1870. In that year, the Red River Rebellion ended and the last Fenian Raid failed. In 1871, with the entrance of British Columbia, the Dominion tightened its hold on the West. The outstanding disputes between the United States and Great Britain were settled by the Washington Treaty in the same year and the Republic accepted, by implication, the accomplished fact of a trans-continental Dominion. It is significant that the departure of the last imperial troops⁸ from Quebec in 1871 did not bring any sudden and vigorous measures for Canadian defence by the Dominion Government. The Dominion was not compelled, after all, to battle for its existence. The political and military purposes which had helped to justify its creation slipped from the minds of a pacific and unapprehensive people.

The Great Depression—check to the Dominion's aggressive program of development and the adoption of the National Policy of protective tariffs.

At the end of 1873, the boom broke and was followed by world-wide depression. In the United States, it involved a sharp contraction in railway and building construction; in Great Britain, a severe contraction of credit and a steep decline in foreign trade. The fall in prices and international lending brought an abrupt check to economic expansion in new countries. In Canada, the first effect of this general depression was a decline in the demand for lumber. Between 1873 and 1879,

⁸ Britain continued to man military stations at Halifax and Esquimaux and the last garrison did not leave Halifax until the beginning of the twentieth century.

exports of forest products fell by one-half. The prices of manufactured goods fell more rapidly than those of agricultural products but by 1876 the country was generally enveloped in depression which grew slowly worse until 1879. In the latter year, both the price level and the physical volume of exports had fallen by 20 per cent from the peak of 1873.

The depression was rapidly translated into falling public revenues while the public debt continued to mount. The Federal Government was driven to serious reconsideration of the extensive projects which had been launched in the preceding prosperous period. Boundless optimism was succeeded by unrelieved gloom. The Government had reaped but little reward for its huge expenditures and it could see no hope of generous returns for years to come. Alarmed at the mounting burden of debt, the Federal Government retreated from its aggressive program of development. The Inter-colonial, the Prince Edward Island railway and the canal improvements were carried to completion. But no new projects were undertaken and, following the Pacific scandals, the agreement for the construction of the Pacific railway was dropped. The new government of Alexander Mackenzie announced a policy of building the railway as a public work but only as the resources of the country would permit.

The Great Depression, which continued almost unrelieved for over twenty years, had serious consequences for the entire country. As time went on, the national policies of the Dominion,⁹ which were to have brought abounding prosperity through western expansion and settlement, were discredited by failure. The men, money and markets, necessary for the successful operation of the expensive national machinery, failed to materialize. The great community equipment lay almost unused, an oppressive burden on the country.

As the depression continued, the old agitation for a policy of protection to domestic industries gathered increasing force and acquired a wider appeal. The tariff policy during the first twelve years was primarily designed for revenue purposes. There was much resentment and dissatisfaction over Confederation in the Maritimes. Among other things, the Maritimes feared an upward revision of tariffs and the Federal Government was anxious to conciliate them by removing any ground for such

fears. Furthermore, the Dominion was anxious not to provoke tariff retaliation by the United States with which Canada enjoyed a growing trade in this period.¹⁰

Thus the early Canadian tariff structure retained the main features, though not the exact rates, of the pre-Confederation tariffs in the provinces. Luxuries paid high rates, the great bulk of finished manufactures paid 15 per cent, raw materials and most semi-finished goods entered free. The only general change in the tariff before 1879 occurred in 1874 when the 15 per cent schedule was raised to 17½ per cent in an effort to maintain revenues in the face of falling imports.

The main object of policy through the period was to get a renewal of the Reciprocity Treaty with the United States. However, the persistent advances to Washington were of no avail. The Washington Treaty of 1871 did not include a renewal of reciprocal trade relationships and the treaty which George Brown negotiated in 1874 was not ratified by the United States Senate. The Washington Treaty gave the Americans free access to Canadian Atlantic fisheries, free navigation of the St. Lawrence and the use of the canals on equal terms. Canada had hoped to bargain for reciprocity with these privileges but the British Government used them to advance the general interests of the Empire. All efforts to secure closer trade relations with the United States failed and the rebuffs aroused in Canada a desire for retaliation.

"Reciprocity of trade or reciprocity of tariffs" became the slogan. There was still no doubt, however, that the former alternative was preferable. American industry had not yet grown up to the protective tariff. It had not yet achieved the special advantage of mass production, and it was handicapped by the high cost of iron and steel and by the inflated wage levels inherited from the Civil War. Canadian manufacturers were agreed that they could compete successfully with the United States producers on the basis of a North American market.¹¹ If, however, they were to be denied this wider market, they insisted that they could not share the limited market at home. If Canadian industry could not develop in relation to an industrial integration of North America, then conditions must be created to enable it to develop in relation to the opportunities of an economic integration of Canada.

⁹ The expression "national policies" as used throughout this Report refers to federal economic policies such as western settlement, all-Canadian transportation and protective tariffs. In the capitalized singular form, the "National Policy" refers solely to the policy of protection adopted in 1879.

¹⁰ This policy was announced in 1868 by the Minister of Finance in his speech on the Budget.

¹¹ See *Canada, Journals House of Commons*, (1876), Appendix (3).

The price decline which began in 1873 was much more pronounced in manufactured goods than in raw materials. Between 1873 and 1879 the price level of Canadian imports (mostly manufactures) dropped 26 per cent while the price level of exports fell by 8 per cent. This, together with the loss of natural shelter resulting from the decrease in transportation costs, bore heavily upon domestic industry and commerce. Declining inventory values inflicted heavy losses upon the distributive trades. The pressure of falling prices and increasing competition led to a general outcry against what was called the "slaughtering of goods" by the United States and Great Britain. Higher tariffs were urged to maintain the balance between imports and the local manufactures. And, of course, there was a more general demand for a protective policy as the panacea for depression.

The high hopes for rapid development of the country and for the commercial and industrial benefits expected to flow from such development were frustrated. While the previous Federal Government had been aggressive in the work of development, the new Ministry was now timid and out of sympathy with the program. In the face of this apparent failure and hesitation, the policy of industrialization by means of the protective tariff was offered as the way out of stagnation, and as a new basis for economic expansion. Under existing conditions, this proposal had a wide popular appeal.

After Confederation, attempts were made to foster a Canadian national spirit, and industrialization by high tariffs was vigorously advocated as an important step in this direction. This particular aspect of the policy was expressed by the Minister of Finance when he submitted the new tariffs to Parliament in 1879. He insisted that "the time has arrived when we are to decide whether we will simply be hewers of wood and drawers of water; . . . The time has certainly arrived when we must consider whether we will allow matters to remain as they are, with the result of being an unimportant and uninteresting portion of Her Majesty's Dominions, or will rise to the position, which I believe Providence has destined us to occupy . . ."¹² The policy which was to transform the economy and make a great nation was impressively labelled "The National Policy".

These various factors combined to bring about a vigorous policy of tariff protection in 1879. The upward revisions of the tariff were comprehensive and were designed particularly to promote domestic

production where imports were large. "We have endeavoured to meet every possible interest . . ." said the Finance Minister. In general, if luxuries be excluded, the highest duties were imposed on finished consumers' goods of widespread consumption, the rates being in the neighbourhood of 30 per cent. The typical rate on fully manufactured industrial equipment and machinery was 25 per cent. Semi-finished goods and industrial materials paid from 10 to 20 per cent. The fact that many of the duties, particularly the most protective, were specific rather than *ad valorem* reflected the recent experience with falling prices.

Textiles, which made up nearly 30 per cent of total imports and in which domestic manufacturing, with the exception of coarse woollens, had made virtually no progress, were specially singled out for a substantial measure of protection.¹³ The added protection given to iron and steel and their products, the domestic production of which was appreciable only in the case of farm implements and the sheltered items (foundry products, certain rolled products and heavy machinery) was confined chiefly to the finished and highly fabricated articles.¹⁴ In the case of primary iron and steel, where imports were heavy, the duties imposed were small.¹⁵ Important items such as furniture, manufactures of glass, chinaware and boots and shoes were given considerable increases in duties.¹⁶ While the bulk of miscellaneous manufactures paid 20 per cent there were many cases of rates equivalent to 30 per cent or over.

The increases in tariffs were also extended to agricultural products but in this case were largely ineffective, because, in most items, the country was on an export basis. A duty of 50 cents per ton was placed on coal and coke to enable Nova Scotia coal to reach the markets of Central Canada which were then being supplied entirely from the United States.

It is clear from this brief analysis that the National Policy tariff of 1879 would be a powerful

¹² Cotton was given protection at all stages of manufacture with duties ranging from 20 per cent on yarns to 34 per cent on piece goods. The tariff on woollens ranged from 29 per cent on yarns to 34 per cent ready-made clothing. Silk piece goods and clothing paid 30 per cent.

¹⁴ Carriages, wagons and railway cars, as well as miscellaneous hardware and tools paid 30 per cent. A rate of 25 per cent was imposed on machinery, farm implements, boilers, tanks and engines, locomotive engines, bridge and structural steel, stoves and castings of all kinds. The duties on equipment and semi-finished articles such as chains, wire, galvanized sheet iron, tin plate and tubing ran from 10 per cent to 20 per cent.

¹⁵ Pig iron paid 12.5 per cent, the principal rolled items (except steel rails) 17.5 per cent, but steel ingots, rails, bars and fish plates remained free.

¹⁶ Furniture and clocks paid 35 per cent, refined petroleum 38 per cent, manufactures of glass 30 per cent, chinaware 25 per cent, woodenware 25 per cent, boots and shoes 25 per cent.

¹³ Budget Speech, March 14, 1879, pp. 22-3.

instrument for promoting domestic production in a wide range of articles and for diverting trade from international into interprovincial channels. With the extension of the protective principle to primary iron and steel by the introduction of bounties in 1883 and higher duties in 1887, the application of the policy was complete. The protective system thus established during 1879-87, although modified and refined, and from time to time changed in its emphasis, has never since been basically altered. It was a drastic change in the conditions under which the economies of the British North American colonies had grown up, and subsequently was a major factor affecting the development and structure of the transcontinental economy which Confederation had created. It became, in truth, a national policy.

Stagnation—unfavourable external influences and the disappointing results of the national economic policies

During the years 1867-79, the three basic national economic policies were adopted. By settlement of the Northwest, transcontinental transportation through all-Canadian territory and industrialization by protective tariffs, the Federal Government planned to bring about economic expansion and complete the unification of the country. Because of the dependence upon exports, foreign capital and immigration, they could become effective only if stimuli came from abroad. For over two decades, however, the external factors were unfavourable. The collapse of the boom in 1873 brought on the Great Depression which continued for twenty-three years. A persistent decline in prices, a sharp shrinkage in international lending and a low level of investment caused general economic stagnation. The Canadian economy, strongly affected by these influences, virtually stood still, although there were many internal shifts and changes.

TABLE 8.—CANADIAN PRICE INDICES, 1871-96

	Wholesale Prices of 70 Com- modities (a)	Ex- port (b)	Im- port (c)	Grains and Flour (d)	Animals and Meats (e)	Iron (f)
1871-73.....	100	100	100 ^(a)	100	100	100
1885.....	79	91	73	93	90	61
1891-93.....	78	97	69	83	94	53
1896.....	85	88	80	83	88	49

^(a) Taylor and Michell, *Statistical Contributions to Canadian Economic History* (Toronto, 1931), p. 56.

^(b) *Ibid.*, p. 6.

^(c) 1873-75 = 100.

The price level, which fell about 35 per cent between 1871-73 and 1896, was a continuous damper upon enterprise. The relatively greater drop in the prices of manufactured goods than in those of raw materials such as lumber and agricultural products was a striking feature of the decline. Thus import prices fell more rapidly than export prices and the terms of trade became increasingly favourable. However, the stimulating effects of this factor upon the exporting groups was largely nullified by the tariff increases of 1879-87.

Domestic production in many lines could not take advantage of the new tariff overnight and thus the most immediate effect of the tariff increases was a substantial rise in Dominion customs revenue. The improvement in Dominion finances coincided with a short period of general economic revival throughout the world from 1879 to 1883. Encouraged by these favourable signs, Sir John A. Macdonald, on his return to power in 1879, took up again the project of a transcontinental railway. The half-hearted policy of building it piecemeal as a public work was discarded and in 1880 a group of capitalists agreed to undertake an all-Canadian railway to the Pacific as a private enterprise.

The Canadian Pacific Railway Company was promised substantial cash subsidies and grants of western lands. A monopoly clause in the agreement practically freed the Company from competition in the area between its line and the American border across Manitoba and the Northwest Territories. Surmounting stupendous difficulties, the railway to the Pacific was completed in 1885. During and after its construction, the Dominion tried to encourage the building of local lines in British Columbia and the Eastern Provinces by means of land grants and cash subsidies. The provinces and the municipalities also gave considerable assistance to railways in the same period. By 1896 this combined public assistance had secured the construction of some 3,300 miles of branch lines and about 1,700 miles of colonization railways.

Under these stimuli, the railway mileage of the country mounted rapidly, despite unfavourable economic conditions. By 1896, there were 16,270 miles of line (one mile per 312 persons, a proportion not much different from that of the present day). In the Maritimes, all the principal lines had been built and a fairly dense network of railways had been laid over the settled portions of Ontario and Quebec.

TABLE 9.—GOVERNMENT AID TO RAILWAYS TO JUNE 30, 1896¹⁷

(Millions of Dollars)	
Dominion	165.0*
Provinces	33.0
Municipalities	16.9
Total	214.9
Total Paid up Capital of Railway Companies, Shares and Bonds	697.2

* In addition the Dominion gave net land grants totalling 31.8 million acres.

An extensive system of branches had been built in southern Manitoba. Slow progress in the North-west Territories had placed lines between Regina and Prince Albert, Calgary and Edmonton and links with the American border ran from Moose Jaw and Medicine Hat. The important role played by governments in the provision of these facilities is indicated in Table 9.

Two generations of North Americans had believed that railways were the unailing cause of general prosperity. But railway expansion did not bring prosperity to Canada in the period under review. The brief trade revival of 1879-83 faded away and the general world improvement of 1888-90 was offset in Canada by poor crops and bank failures. The Great Depression did not lift until 1896 and it was not until 1897 that the per capita volume of exports reached the level attained in 1873.¹⁸

17	
Dominion	
Construction—	
Intercolonial and P.E.I. Railways	59.0
Canadian Pacific Railway	37.7
Other railways5
	97.2
Subsidies—	
C.P.R. main line and main line exten- sions	28.0
Allowance for C.P.R. lands	10.2
Other railways	13.6
	51.8
Loans	16.0
Total Dominion Aid	165.0
Provinces	
Subsidies and Construction	27.1
Loans	5.6
Subscription to shares and bonds3
Total Provincial Aid	33.0
Municipalities	
Subsidies and Construction	11.7
Loans	3.0
Subscription to shares and bonds	2.2
Total Municipal Aid	16.9
Total Government Aid	214.9

¹⁸ During 1888-90, the volume of exports per capita was 20 per cent below the level of 1871-73.

The changes in the composition of exports reveal some of the internal shifts in occupations that took place under the downward pressure. Lumber declined in relative importance while agriculture continued to expand. But here there was a shift from grains, which met the rising American tariffs and stiffer competition from the American West, to live stock and dairy products which, with cheaper transportation, found larger markets in Great Britain. Increasing exports of fish reflected the development of the salmon fishery in British Columbia and the lobster fishery in the Maritimes. Particularly after 1886, they also reflected the pressure of people crowding into the industry as a means of livelihood owing to the virtual disappearance of shipbuilding and shipping.

TABLE 9A.—EXPORTS OF CANADIAN PRODUCE, 1868-1896
(Millions of Dollars)

Years ending June 30	Total	Agricultural Products			Products of the Forest	Fish	Minerals	Manufactures and Miscellaneous
		Animals and Their Produce	Grains, Vegetables, Fruits etc.	Total				
1868	48.5	6.9	12.9	19.8	18.7	3.4	1.3	6.3
1874	76.7	14.7	19.6	34.3	27.2	5.3	3.8	6.1
1879	62.4	14.1	19.6	33.7	13.3	7.1	3.2	5.1
1882	94.1	20.5	31.0	51.5	24.0	7.7	3.1	7.8
1886	77.8	22.1	17.7	39.8	21.0	6.9	4.1	6.0
1891	88.7	26.0	13.7	39.7	24.3	9.9	6.0	8.8
1896	109.7	26.5	14.1	50.6	27.2	11.2	8.4	12.3

The effect on Canada of the adverse economic conditions between 1874 and 1896 is most clearly revealed by the population figures. The principal policies and expenditures of the Federal Government were designed to fill the empty spaces with people. Yet for thirty years Canada was a land of emigration helping to people the frontier and cities of the United States.

TABLE 10.—CANADIAN POPULATION MOVEMENTS, 1871-1901
(Thousands)

—	Population at beginning of Decade	Actual Increase	Natural Increase (Est.)	Immigration	Emigration (Est.)
1871-81	3,889	636	799	342	506
1881-91	4,325	508	686	886	1,064
1891-1901	4,933	538	613	321	295

In each of the three decades, 1871 to 1901, as indicated by Table 10 the increase in Canadian population was less than the estimated natural increase. While slightly more than one-and-a-half million immigrants intending to settle entered Canada, almost two million people left the country. Between 1881 and 1901 over 600,000 native Canadians moved across the border and in 1891 about one-fifth of all the Canadian-born lived in the United States. So heavy was the emigration in the early nineties that the population was virtually stationary.

The disappointingly slow growth of population between 1871 and 1901 was accompanied by significant changes in its distribution. Owing to improvements in transportation and growing industrial development, Canada was losing its predominantly rural character. The urban population rose from 20 per cent of the total to 38 per cent. The towns and cities absorbed 77 per cent of the total increase in population. At the beginning of this period, Montreal and Toronto, serving the hinterland of the St. Lawrence Valley, had 5 per cent of the total population. In 1901, with a greatly extended hinterland, the proportion had risen to 10 per cent.

Regional and Provincial Discontent—the challenge to the dominance of the Dominion

A bald statement of the length of the depression gives little hint of its effect upon the lives of the people. Federal policies had burdened them with debt and failed to bring prosperity. The only large-scale remedy which the Dominion had been able to offer was the National Policy of 1879. In these circumstances, communities had to do what they could to help themselves, looking to the provinces for the help which the Dominion failed to give. The provincial governments attempted to promote expansion on their own frontiers by railway building and immigration policies. But most of them quickly discovered the strait jacket in which the financial settlement of Confederation had placed them. The agitation for better terms gathered strength and led to differences with the Dominion. The failure of the Dominion's economic policies, which formed such important elements in the new national interest, discouraged the growth of a strong, national sentiment; and local loyalties and interests began to reassert themselves.

Indeed, there had never been any large transfer of loyalty from the older communities to the new Dominion created for urgent common purposes. The achievement of Confederation and the

spectacular activity of the Federal Government in the early years had merely overshadowed or, at most, temporarily subordinated the separate interests of the distinct regions and communities. From the very date of the union, there had been a widespread and burning conviction in Nova Scotia that it had been manoeuvred into a bargain prejudicial to its vital interests. In the provincial election held late in 1867 thirty-six out of thirty-eight members elected to the legislature were anti-Confederates. The new Government tried desperately to extricate the Province from the bonds of the union. Although these efforts were unavailing, the sentiment against Confederation remained strong in Nova Scotia and was significant in New Brunswick.

Confederation had not succeeded in eliminating the clash of racial and religious differences which had agitated the Province of Canada in the past. It had been hoped that the creation of two provinces, allowing free play to these cultural differences in separate spheres, would remove these antagonisms from deliberations on matters of common interest in the federal councils. When the western insurrections of 1870 and 1885 raised a racial and religious conflict in the valleys of the Red River and the Saskatchewan which disturbed the peace in the new federal territories, the opinions of the dominant groups in Ontario and Quebec clashed over the action taken by the Federal Government. Quebec's deepest feelings were outraged by the execution of Louis Riel and a wave of resentment against the Federal Government swept the Province. It became clear at once that there were federal issues in which conflicts of opinion might follow in the main provincial lines. In such circumstances, any solution was bound to create Dominion-provincial friction.

Such Dominion-provincial friction was not limited to cases of the resurgence of loyalties antedating Confederation. The problems of the Pacific railway embittered the relations of British Columbia and the Federal Government during the seventies; and in the eighties the requirements of federal railway policy brought Manitoba and the Dominion into sharp conflict. The appropriation of western lands "for the purposes of the Dominion" deprived Manitoba of its natural resources and the monopoly clause in the charter of the Canadian Pacific Railway Company prevented the Province from promoting a competitive transport system. Repeatedly the Provincial Legislature chartered railway companies to build lines to the international boundary and repeatedly the Dominion Govern-

ment disallowed them on the ground that the projected lines would divert traffic to the United States and thus conflict with the settled transport policy of the Dominion. Dominion policy was hard to reconcile with the interests of the settlers in Manitoba and the Provincial Government became the spearhead of local demands.

British Columbia was irritated by federal tariff policy and its long controversy with the Dominion over Oriental immigration began in this period. Large sections of opinion in the Maritimes were antagonized by the introduction of the National Policy in 1879. In 1886, a series of resolutions was introduced in the Legislature of Nova Scotia advocating secession on the ground that the commercial and financial interests of the Province had been vitally injured by Dominion policies. By 1887, agricultural and lumbering interests in Ontario were straining against federal tariff policy and urging commercial union with the United States. Ontario clashed with the Dominion over the location of the Ontario-Manitoba boundary and the ownership of its northern natural resources. Mowat, as Premier of Ontario, fortified the principle of "provincial rights" when he claimed and won the right of the provinces to regulate the sale of liquor within their boundaries and for years he conducted an unwearying attack on the federal power of disallowance.

These various grievances culminated in the provincial conference held at Quebec in 1887. The five provincial premiers who attended included all the leaders of provincial protest. The procedure of the provincial premiers seems to indicate that they claimed the right to examine and correct the operation of the federal system. Although their interests differed widely, they were able to agree that a considerable curtailment of federal power would be desirable. They proposed to increase the subsidies to the provinces, to abolish the federal power of disallowance, and to make the right of the Dominion to declare public works to be for the general advantage of Canada conditional on the approval of the province concerned. Lieutenant-Governors were to be acknowledged to be representatives of the Sovereign rather than of the Dominion, and each province was to nominate half of the Senators from the province in the Senate.

The conference challenged the view that Confederation was designed to set up a highly centralized and pervasively dominating government at Ottawa. In its swing to the other extreme, emphasizing the primacy of the provinces, it was no doubt employing a theory of federalism similar

to the doctrine of "states' rights" in the United States. But the strength and diversity of provincial interests shown by the conference indicated that, under the conditions of the late nineteenth century, the working constitution of the Dominion must provide for a large sphere of provincial freedom.

The policies of the Federal Government were in discredit and the Government itself was embarrassed by its difficulties in the late eighties. Except for a short interval between 1874-78, the Federal Government throughout this period had been identified with Sir John A. Macdonald and his associates. Sir John's views of the nature of Confederation, so clearly stated both before and after the union, are well known. It is not known how many of the other framers of the British North America Act shared his views. But it is important that, for nearly thirty years, Macdonald and those who thought like him were the Federal Government of the new Dominion. The views which they took of the functions of the Lieutenant-Governor and the use to be made of the powers of reservation and disallowance have already been discussed. Their practice in revising the financial arrangements with the provinces and securing constitutional amendments has been noted. Their actions reveal clearly their conception of the primacy of the Dominion and the subordinate position of the provinces.

It is highly significant that the realities of the later years of the period forced a modification of this conception on the very men who held it most strongly. Their interpretation of the general interest failed to command widespread assent in the different provinces. The ineradicable, particularist interests, always associated with different regions and ways of life, demanded free expression. In face of the formidable provincial protest, the Government was forced to retreat. In 1884, the Ontario Rivers and Streams Act, already thrice disallowed by the Dominion, was re-enacted by the Provincial Legislature and the Dominion acquiesced. Later, the Dominion abandoned its policy of protecting the Canadian Pacific Railway Company from competition through the power of disallowance and finally repealed the monopoly clause itself. During the early nineties, it began the downward revision of the tariff.

Provincial Rights and the Constitution—the interpretations of the Privy Council widen the powers of the provinces.

It is a matter for speculation what would have been the ultimate issue between the Dominion

and the provinces if the conditions of the eighties had continued. The equilibrium was becoming very unstable. On the one hand, there was the conception of federal dominance which the Dominion Government tried to enforce and which was strongly supported by powers of reservation and disallowance. There were the sweeping words of the opening paragraph of section 91 which, it might be argued, gave to the Dominion those "high functions and almost sovereign powers" which at least some of the framers intended it to have. The power to tap all the really productive sources of revenue was in the hands of the Federal Government.

On the other hand, there was the patent failure of the great general projects of the Dominion to meet what the provinces deemed to be their particular interests. There was the provincial revolt, focused by the provincial conference of 1887, which significantly demanded a drastic reduction of federal powers. There were straitened provincial governments representing large bodies of opinion and demanding greater revenues.

The preamble of the British North America Act announced the formation of a federal union, but it was not clear how far this was consistent with the wide general powers conferred on the Dominion by the opening words of section 91. Dominion-provincial friction was not lessened by these seeming obscurities in the constitution. It was becoming vital to know what the constitution meant and whether it could be harmonized with the realities which had appeared. In this crucial decade, the Privy Council began to give its first important decisions on the British North America Act. By the end of the period under review, the main lines of the working constitution had emerged through these decisions. It is therefore necessary to turn to them to see how the constitution was moulded by their influence.

It would be difficult to say how far these decisions influenced the concessions made by the Federal Government. At any rate, some of the earliest of these cases bore on the nature of the provincial governments and their relation to the Dominion and to the Crown. In particular, decisions in 1883 and 1892 denied some of the main tenets of the Macdonald school. In *Hodge v. The Queen*, in 1883, their Lordships, by implication, denied that the provincial legislatures were inferior bodies. They held that, within the limits of subjects and areas as prescribed by section 92, "the local legislature is supreme and has the same authority as the Imperial Parliament

or the Parliament of the Dominion, would have had under like circumstances"²⁰ to confide powers to bodies of its own creation.

In *Liquidators of the Maritime Bank v. Receiver-General of New Brunswick* in 1892, it was necessary to decide how far the provincial Executive was entitled to exercise the ancient prerogatives of the Crown. In answer to the argument that the British North America Act had severed all connection between the Crown and the provinces and reduced the latter to the rank of Liverpool or Manchester, the Privy Council replied that the provinces were not subordinated to the Federal Government or depreciated to the level of municipal institutions. The supremacy of the province in its field of jurisdiction was reiterated. Their Lordships were pressed to say that, as the Lieutenant-Governor was appointed by the Dominion, he was purely a creature of the Dominion. Lord Watson denied this conclusion saying that the Governor General, in appointing, was acting for the Queen and that a "Lieutenant-Governor, when appointed, is as much the representative of Her Majesty for all purposes of provincial government as the Governor-General himself is for all purposes of Dominion government".²²

These decisions magnified the provinces and struck at the theory that they were merely a superior kind of municipal institution. They also raised acutely the question of how far the enactments of a legislature endowed with the same kind of supremacy as the Imperial Parliament should be subject to an unrestricted power of disallowance. These decisions, at least, made it harder for the Federal Government to maintain its positions and foreshadowed the steep decline in the use of the powers of reservation and disallowance which came in succeeding years.

A detailed review of the Privy Council decisions of this period would be out of place here. But there were several cases of historic importance in determining the lines of constitutional development which must be considered. In 1882, the Privy Council had to decide whether the Canada Temperance Act was within the powers of the Dominion. This Act forbade the sale of intoxicating liquor under penalty of fine and imprisonment in those municipalities which exercised the "local option" of applying its provisions.

Naturally, it was argued that this prohibition would interfere with property and civil rights in

²⁰ (1883) 9 A.C. 117, at p. 132.

²² [1892] A.C. 437, at p. 443.

the local areas where it was adopted. However, the Act recited the desirability of uniform legislation promoting temperance throughout the Dominion and the Privy Council concluded that the traffic in liquor was being dealt with as a matter of public order and safety and not in relation to the aspects of property and civil rights which were admittedly involved. They decided that general liquor legislation so conceived was exclusively within the general power of the Federal Parliament "to make laws for the peace, order and good government of Canada". General legislation, genuinely "deemed to be necessary or expedient for national safety or for political reasons" or "designed for the promotion of public order, safety or morals", was held to fall within the general power of section 91. Of course, in almost every case, such legislation would "in some incidental way, affect property and civil rights". Thus, "the true nature and character of the legislation in the particular instance under discussion must always be determined in order to ascertain the class of subjects to which it really belongs".²⁴

This decision asserted the clear primacy of the "peace, order and good government" clause over section 92 and argued the validity of all federal laws dealing with general and national aspects of any subject matter even though that subject matter, in its local aspects, might be within the enumerations of section 92.²⁵ However, it left the criterion of what might be "necessary or expedient for national safety or for political reasons" and of what might be "designed for the promotion of public order, safety and morals", vague and unsettled. Such questions as these could only be determined by reference to the political, economic and social conditions of the time and to certain broad considerations bearing on the problem as to what it is proper for governments to try to do.

The decision did not explain how "the true nature and character of the legislation in the particular instance" was to be determined. There were only two alternatives. Either the existence of that urgent general or national aspect which was to justify untrammelled federal legislation under the "peace, order and good government" clause should be decided by the court before which the validity of the legislation was raised, or it would have to depend on the simple assertion of national urgency by the Federal Parliament.

²⁴ *Russell v. The Queen* (1882) 7 A.C. 829, at pp. 838-40.

²⁵ Although *Russell v. The Queen* is frequently cited in the courts, the general principle which it lays down has not been followed and it must be regarded as virtually over-ruled by later decisions.

In the first event, the court would be required to say whether the federal legislation in question had such a general or national aspect—in short, whether, in view of all the circumstances, the legislation might conceivably be desirable in the national interest. But this is a question which the courts always dislike to answer on the sound ground that it is not a question of law at all. The answer, if given, would inevitably depend upon the temperament of the judge and his personal views on public policy. Judges, like other people, differ profoundly in their views on public policy and their decisions would become essentially unpredictable. The hope of drawing a clear line between the legislative sphere of the Dominion on the one hand, and that of the provinces, on the other, would disappear. Moreover, because the principal test of the validity of provincial and Dominion legislation would be the judgment of the court on large issues of expediency and public policy, the final court of appeal would become the arbiter of public policy rather than the guardian of the constitution and, therefore, the storm-centre of Dominion-provincial disputes.

The court might escape from this invidious task by limiting itself to the question of whether the Federal Parliament had decided, in good faith, that general and national aspects were involved. Careful reading of *Russell v. The Queen* gives some reason for thinking that the personnel of the Privy Council in that case conceived its duty to be discharged by this limited scrutiny. In the nature of things, it would be a rare case where bad faith on the part of the Federal Parliament could be established and therefore the first alternative might, in practice, come to little more than the second, which is now to be considered.

The second alternative would be that the bare assertion by the Federal Parliament of a general or national aspect in the subject matter of the legislation would, of itself, justify the legislation under the "peace, order and good government" clause. That clause would then confer tremendous power on the Federal Parliament, giving it, as Macdonald had proposed, "the general mass of sovereign legislation".³¹ The exclusive sphere ensured to the provinces by section 92 might, if the Dominion so desired, become very small indeed. The power of the Dominion Parliament under the "peace, order and good government" clause would become so overwhelming that the federal character of the constitution would be open to grave doubt. Indeed, under these conditions, the constitution in its working, would approach the legislative union which

³¹ *Confederation Debates*, p. 41.

some of the Fathers desired but which, as they recognized, they could not secure by agreement.

These implications of *Russell v. The Queen* must be kept in mind and related to the growing revolt of the provinces against the paternalism of the Dominion when considering the case now to be discussed. "The Local Prohibition Case",³² as it has come to be called, which was decided in 1896, is the most important case in the period, and one of the most significant of all interpretations of the British North America Act by the Privy Council. In it, the Privy Council upheld the validity of the Ontario Temperance Act which provided for Ontario a structure of regulation of the liquor traffic similar to that which the Canada Temperance Act provided for the Dominion as a whole.

The technique of interpretation used to reach this result need not be discussed here. It is sufficient to say that while Lord Watson held that the Dominion, relying on the enumerated heads of section 91, could validly enact legislation which affected subjects enumerated in section 92, he also declared that the Dominion, when legislating under the general "peace, order and good government" clause, "has no authority to encroach upon any class of subjects which is exclusively assigned to the provincial legislatures by s. 92". He stated that the exercise of legislative power under the general clause of section 91 must be "strictly confined to such matters as are of unquestionably Canadian interest and importance", admitting that "some matters, in their origin local and provincial, might attain such dimensions as to affect the body politic of the Dominion and to justify the Canadian Parliament in passing laws for their regulation or abolition in the interest of the Dominion".³⁴ Under the authority of this decision, the general clause of section 91 has come to be regarded as justifying little more than emergency legislation in the stress of great national crises.

While not challenging the correctness of *Russell v. The Queen*, this decision struck directly at the reasoning on which it was based. It denied the primacy of the "peace, order and good government" clause of section 91 over the enumerations of section 92 and as a result Dominion jurisdiction became, for most purposes, restricted to the specific heads enumerated in section 91. In the main, interpretation of the legislative powers of the Dominion and the provinces settled down to a competition between the specific enumerated heads

of sections 91 and 92. In this competition, the provinces enjoyed an advantage because section 92 contained two heads capable of a general and inclusive signification, viz., "Property and Civil Rights in the Province" and "generally all Matters of a merely local or private Nature in the Province" while section 91 contained only one such head, "the Regulation of Trade and Commerce" and, as will be pointed out below, it received a restricted interpretation. Thus the stage was set for the subsequent course of interpretation which has provoked the comment, in recent times, that the residuary powers under the constitution are now to be found in section 92.

There are some who believe that the Local Prohibition Case involved a textual violation of section 91 of the British North America Act.³⁵ Logical exposition, limited to sections 91 and 92, might lead to that conclusion. But it must be remembered that, according to the preamble of that Act, what was desired by the provinces was a federal union. It has been pointed out that the decision in *Russell v. The Queen*, which, in practical effect, was over-ruled by the Local Prohibition Case, would have imperilled the federal character of the union if it had become the ruling decision. There seems to be no doubt that this consideration weighed heavily with Lord Watson. In an earlier case, he had pointed out that "the object of the Act was neither to weld the provinces into one, nor to subordinate provincial governments to a central authority, but to create a federal government . . . each province retaining its independence and autonomy".³⁶ In justifying his construction of sections 91 and 92 in the Local Prohibition Case, he made the following significant statement:—

"To attach any other construction to the general power which, in supplement of its enumerated powers, is conferred upon the Parliament of Canada by s. 91, would, in their Lordships' opinion, not only be contrary to the intentment of the Act, but would practically destroy the autonomy of the provinces. If it were once conceded that the Parliament of Canada has authority to make laws applicable to the whole Dominion, in relation to matters which in each province are substantially of local or private interest, upon the assumption that these matters also concern the peace, order, and good government of

³² The most cogent and complete statement of this view is to be found in the Report pursuant to Resolution of the Senate to the Honourable the Speaker, by the Parliamentary Counsel relating to the Enactment of the British North America Act, Ottawa, 1939. For criticism see V. Evan Gray, *Canadian Bar Review*, 17, p. 309.

³³ *Liquidators of the Maritime Bank v. Receiver-General of New Brunswick*, [1862], A.C. 437 at pp. 441-2.

³⁴ *Attorney-General of Ontario v. Attorney-General of the Dominion*, [1896] A.C. 343.

³⁵ *Ibid.*, pp. 360-61.

the Dominion, there is hardly a subject enumerated in s. 92 upon which it might not legislate, to the exclusion of the provincial legislatures."³⁷

It may be that the insight which guided his decision was solely derived from a theoretical analysis of the requisites of a federal state. It may be that he was also aware of the growing provincialism, then assailing the pretensions of the Federal Government. At any rate, he perceived and stated the lines of what he regarded as a tolerable compromise between Dominion power and provincial claims in the Canada of his day. And compromise is always the essence of the federal state.

It is necessary to notice briefly a foreshadowing in this period of the limited interpretation later given to the Dominion power under head 2 of section 91, "the Regulation of Trade and Commerce". In a case before the Privy Council in 1881, the question of the meaning to be attached to this phrase was considered. Their Lordships pointed out that the words "regulation of trade and commerce", in their unlimited sense are sufficiently wide, if uncontrolled by the context and other parts of the Act, to include every regulation of trade . . . down to minute rules for regulating particular trades".³⁸ By a process of textual criticism for which the enumerated heads of section 91, taken as a whole, give some warrant, they reached the conclusion that the words were not used in their unlimited sense,³⁹ and suggested limitations which were later adopted and pushed still further by the courts. The case also made a significant contribution to the interpretation of head 13 of section 92, holding that, in the phrase "Property and Civil Rights in the Province", the expression "civil rights" includes rights arising from contract as well as rights directly maintained by the law itself such as the status of persons.

³⁷ *Attorney-General of Ontario v. Attorney-General of the Dominion*, [1896], A.C. 348 at p. 361.

Lord Watson assumes, it is to be noted, that, if *Russell v. The Queen* remained the ruling decision, the Privy Council would shrink from deciding whether particular Dominion legislation might be "necessary or expedient for the national safety or for political reasons" and would in practice, leave that question to the discretion of the Dominion Parliament—in other words, the second alternative discussed above would rule. In these circumstances, it is not surprising that the Privy Council exerted itself to make the specific and more concrete enumerations of section 91 the main test of the validity of Dominion legislation.

³⁸ *Citizen's Insurance Co. v. Parsons* (1881), 7 A.C. 96, at pp. 112-13.

³⁹ Their reasons for thinking so are given in *Bank of Toronto v. Lamb*, (1887), 12 A.C. 575 at p. 586, where it is said that in *Parsons Case*, "it was found absolutely necessary that the literal meaning of the words ["regulation of trade and commerce"] should be restricted in order to afford scope for powers which are given exclusively to the provincial legislatures."

One other case, relating to the taxing power of the provinces, requires to be considered. Section 92 gave the provinces a power of "Direct Taxation within the Province in order to the raising of a Revenue for Provincial Purposes". In 1882, the Quebec Legislature passed a statute imposing on certain commercial corporations, a tax the amount of which varied with the paid-up capital and the number of places of business. A number of corporations resisted collection of the tax and an appeal was finally taken to the Privy Council.⁴⁰ Their Lordships were obliged to decide whether or not it was a direct tax.

"Direct taxation" is a phrase which lacks precise signification. From an economic point of view, it is impossible to say that any particular tax is direct in its final incidence because of the opportunities which may exist for shifting its burden. Economists would agree that a corporation tax generally is an indirect tax because of the ease of shifting it. However, the Privy Council felt bound to find a criterion for the validity of provincial taxation which would not involve the impossible task of trying to find out, in each case, whether the burden had, in fact, been shifted.

Adopting from John Stuart Mill a statement that "a direct tax is one which is demanded from the very persons who it is intended or desired should pay it", they inferred from the legislation itself that the legislature must have intended it to be finally borne by the very corporations from whom it was demanded and held it to be "direct taxation" within the meaning of section 92. The decision was one of great significance. From the point of view of the provincial governments it made available an important and increasing source of revenue since corporate enterprise was expanding rapidly. From the point of view of the economy as a whole it was the legal basis of the growth of much of the duplication, confusion and uneconomic types of taxation which today weigh oppressively on the national income.

2. PUBLIC FINANCE, 1867-96

The Financial Settlement on Trial—an extremely tight fit for the Maritimes and revisions of the formula

Confederation began auspiciously for the public finance operations of the Dominion. World prosperity spurred on a large program of development. Imports rose rapidly and the taxation system, geared so sensitively to import trade,

⁴⁰ *Bank of Toronto v. Lamb*, (1887), 12 A.C. 575.

responded in an impressive manner. Customs receipts rose from \$9 million to \$14 million, and excise revenues, from luxury consumption, from \$3 million to \$5½ million between 1867 and 1874. This increase of more than 60 per cent in taxation revenues in a short period of seven years made possible the "rounding-out" of the Confederation scheme already discussed. The Dominion Government was proving to be a magnificent financial instrument for creating the new British North America of which the Fathers had dreamed.

On the other hand, there was a wide variation in the financial condition of the provincial governments in the early years after Confederation. At first, Quebec was in a relatively easy, and Ontario in an even more comfortable position, while New Brunswick, and particularly Nova Scotia, were, from the beginning, in very straitened circumstances. The allocation of functions and revenues discussed at Quebec in 1864 meant roughly that the provinces would be left with \$1½ million of local revenues to meet an estimated \$4 million of local outlay while the Dominion was to be given \$12 million in revenue to meet less than \$9 million in outlay. It was proposed to balance the provincial budgets by transferring \$2½ million to the provinces in the form of federal subsidies. The total amount of the agreed subsidies was sufficient to bridge the estimated gaps but the current conception of equity which required calculation of subsidies on a per capita basis glossed over real differences in need arising from disparate circumstances, unconnected with differences in population. The result of the settlement was that Ontario and Quebec got subsidies greater than their needs at the time. For several years, Ontario had considerable surpluses while the position of Nova Scotia became intolerable as early as 1868.

As already mentioned, Tupper had promised at Quebec that Nova Scotia would make ends meet somehow on a subsidy of 80 cents per capita, yielding \$264,000. Even when supplemented by the grant of \$60,000, in support of legislature and government, agreed on at London, Nova Scotia was still unable to honour Tupper's promise. The "better terms" agreement of 1869 gave the Province an additional \$140,000 of which \$83,000 was for a ten year period only.

In 1873, the Dominion assumed the "excess debt" of Ontario and Quebec. The consequent proportionate increase in the debt allowances of the other provinces afforded some further relief to Nova Scotia. However, with the expiry of the temporary grant in 1877 and the withdrawal by the Province

of capital sums on debt allowance account, Nova Scotia's subsidy, in spite of other minor additions, had fallen to \$433,000 by 1884, at which figure it remained until 1906. The revenues from public domain did not expand as expected, municipal organization lagged and political considerations discouraged the introduction of direct taxation. Appeals to Ottawa for further subsidy increases were fruitless and throughout the period under review, Nova Scotia was seriously cramped by its inelastic revenue system.

New Brunswick had made a rather better bargain at Confederation and also improved its position slightly when it commuted its export duty on lumber for a subsidy of \$150,000 a year. But apart from these minor reliefs and particularly after its special temporary grant expired in 1877, its position was on all fours with that of Nova Scotia. Indeed, it was more heavily dependent on the Dominion subsidy for its revenues than was Nova Scotia.

The impossibility of dealing fairly with dissimilar areas and conditions by use of a common formula was revealed again in the financial settlements with the new provinces which entered the union early in this period. The Red River Settlement which had chafed under the rule of the Hudson's Bay Company but lacked experience in managing its own affairs suddenly blossomed into the Province of Manitoba in 1870. In substance, it was a creature of the Dominion Government without a will of its own and consequently the formula used in calculating the amount of subsidies for the four original provinces was strictly applied to it. As a result of the arrangement with Nova Scotia in 1869, the debt allowance had been raised from \$25 to \$27.77 per capita. Manitoba's population of 12,000, of whom less than 2,000 were whites, was generously assumed to be 17,000. Thus the Province was given the subsidy of \$67,000 to which it was entitled according to the formula.

Other provinces were expected to supplement their revenues from the public domain but Manitoba's lands were reserved by the Dominion to aid the federal policy of development. Yet the Province was not compensated for their retention. Lacking taxable capacity and having virtually no other revenue, the province was unable to support its governmental structure and it is not surprising that the annual subsidy was increased on four separate occasions during the next fifteen years.

Actual need and political expediency brought a considerable modification in the application of the formula to British Columbia and Prince Edward

Island. Strict application of the formula to British Columbia in 1871 would have given a subsidy wholly inadequate either to replace the customs revenue which was being surrendered to the Dominion or to meet the financial needs of the Province. British Columbia contended that its customs collections were equal to the amount of customs revenue derived from 120,000 people in the Eastern Provinces and suggested that the 9,000 whites and the 25,000 Indians and Chinese in the Province be regarded, for the purpose of subsidy, as a population of 120,000 and that the subsidy be calculated accordingly. This was not acceptable to the Dominion but another device was invented which served much the same purpose and British Columbia was brought into the union with a subsidy of \$216,000 a year instead of the \$75,000 which a rigid application of the formula to the actual population would have given.⁴¹

In 1873, Prince Edward Island secured a settlement involving a more radical revision of the formula. The public debt of the Province had rushed upward between 1867 and 1873. In order to lift the burden of debt charges from the Province, it was necessary to calculate the debt allowance at \$50 per capita. In addition, the fact that the Province had no public lands induced the Dominion to give a further subsidy in lieu of lands. The original formula would have yielded a subsidy of only \$45,000 but with these modifications, the Province secured an annual grant of four times as much.

Within a short period of time, these settlements in turn proved inadequate. In the eighties, Quebec also got into financial difficulties and, by 1887, all the provinces except Ontario were clamouring for an increase in subsidies. No further alterations were made during this period. The reasons why these adjustments and concessions, which had seemed adequate at the time, failed to meet the fiscal needs of the provinces will be considered later when the provincial revenues and expenditures are reviewed.

The Finances of the Dominion—concentration on economic development

The Federal Government had taken over the pre-Confederation debts of the provinces and was expected to finance the new program of development, to provide for defence and to assume the major burden of general government and legislation. The budgets of this period show that these expectations were being substantially realized.

⁴¹ For extended discussion of subsidy arrangements with British Columbia see Book II, Section F, Ch. II.

Virtually all the Dominion debt accumulated between 1867 and 1896 was incurred for development. By paring expenditures on general government and taking advantage of its freedom from large expenditures for defence which weighed so heavily on European governments, the Dominion was able to concentrate its efforts on this single activity. In 1874, at the end of the first spurt of development, debt charges and current outlay on transportation, agriculture and public domain accounted for half the current expenditures. The building of the Canadian Pacific in the early eighties added considerably to the total liabilities. In the general depression which descended again after completion of the road, the Dominion found its debt charges embarrassing and did not undertake any further large developmental program in this period. Nevertheless, in 1896, these same items still absorbed almost half the current outlay, while defence and general government accounted for only 6 and 28 per cent respectively. The traditional role of government in British North America as an agency for creating conditions in which private enterprise might thrive had been assumed by the Dominion. In this respect at least, the Dominion was living up to the original conception of its purpose.

But the ability of the Dominion to carry through the developmental program fluctuated greatly because of its heavy dependence on customs revenue. Until the Great War (1914-18), the financial fortunes of the Federal Government were directly and completely linked to the ups and downs of international trade and investment. As revenues rose with rising imports, the Dominion embarked on large developmental expenditures. This involved the investment of foreign capital, which entered the country in the form of goods. The increase in imports at once swelled the customs revenue. Meanwhile, investment stimulated internal activity, increasing employment, raising wages and consequently improving domestic trade. This increase in domestic trade boosted excise revenues.

Therefore, one of the first effects of a program of development was to fill the Dominion treasury and the government tended to forget that it increased the debt as well. In an optimistic mood, it raised its commitments for development still further. As long as investment funds were forthcoming, this procedure could continue almost indefinitely. However, because the flow of investment was certain to be checked at some time, a thoroughly false position was being built up.

The moment the inflow of capital ceased, imports fell sharply, customs revenue slumped, employment declined, the consumption of liquor, tobacco and other luxuries fell away, excise revenues collapsed and the Dominion suddenly found itself with a heavy deficit. Meanwhile, the outlays on development had substantially increased debt charges, thus adding to the rigid and uncontrollable expenditures. In the sequel, it became more difficult to balance the budget by the familiar methods of retrenchment and higher taxation.

The embarrassing stages of the first of these cycles coincided roughly with Alexander Mackenzie's tenure of office. The Ministry of Sir John A. Macdonald experienced a similar cycle in the eighties, which was initiated by the expansion attending the construction of the Canadian Pacific railway. In the years 1881, 1882 and 1883, the Dominion enjoyed remarkable surpluses on ordinary account.⁴³ Relying on these temporary surpluses, the Government devoted a larger sum than ever before to public works (including buildings and harbours) in 1883-84 and embarked on a scheme of cash subsidies for railway construction. Then the flow of investment slackened, the peak surplus of over \$8 million reported in 1884 was wiped out by rising expenditure a year later and by 1886 was converted into a substantial deficit.

The public finance system was still sufficiently flexible to enable Ministers of Finance, by increased taxation and economy, to balance their budgets in a short period. Deficits reappeared in the early nineties which were more difficult to wipe out. The persistent fall in prices due to economic stagnation affected seriously the yield of *ad valorem* customs duties. In 1895, customs receipts were \$5½ million below what they had been in 1883, while debt charges and other government expenditures were slowly but stubbornly rising. Under such circumstances the enthusiasm for an aggressive program of development disappeared. The results of past efforts were disappointing in the extreme and now the Dominion could do little more than carry the commitments it had already undertaken.

*The Straitened Circumstances of the Provinces—
the growth of expenditures and the slowness of
municipal development*

The financial settlement at Confederation had left the provincial governments almost entirely

dependent upon federal subsidies and the revenues from licences, fees and the public domain. It was expected that the receipts from the public domain would expand sufficiently to enable the provinces to extend their existing services to a growing population. Direct taxation was held to be impracticable and thus the expansion of activities would be restricted. Municipal organizations, it was expected, would assume an increasing share of the governmental burdens.

Municipal development lagged, however, except in Ontario. The Maritimes were slow to introduce a system to which they were not accustomed. Some progress was made in Quebec and Manitoba but very little in British Columbia. Failure to make rapid progress in this direction increased the financial difficulties of these provinces. In Central Canada, where urbanization was rapid, where the number of cities of over 10,000 in population doubled and the population of Montreal and Toronto doubled and trebled respectively in this period, municipal activities and expenditures expanded greatly. The provincial government of Ontario, and to a certain extent that of Quebec, derived considerable financial relief from the growth of local governments which provided a large share of the necessary services out of levies on real estate.

Although in most provinces municipal development was slow, provincial governments confined by their narrow revenue systems did not increase their expenditures greatly. Between 1874 and 1896, the total per capita outlay of all the provinces rose only from \$1.69 to \$2.20. This restraint on provincial outlay during a long period of depression was made tolerable by the nature of the economy of the time. The relative self-sufficiency of the family and local communities enabled individuals to weather the depression somehow without reliance on governments. Those who were unable to make adjustments in this way were forced into the stream of migration to the south where they were absorbed by the rapid industrial development and the expanding frontier of the United States. In the 1930's, when self-sufficiency had sharply declined and emigration was stopped, it proved to be no longer possible to hold down governmental expenditures in face of a prolonged major depression.

⁴³ An increase in customs receipts of \$520,000 on a single group of commodities was largely attributed by the Minister of Finance to imports of locomotives, railway carriages and coal for the Canadian Pacific Railway.

TABLE 11.—GOVERNMENT EXPENDITURES ON CURRENT ACCOUNT^(a), 1874 AND 1896
(Thousands of Dollars)

	Provinces		Dominion		Total Provinces and Dominion	
	1874	1896	1874	1896	1874	1896
Net Debt Charges.....	—	1,526	5,373	9,483	5,373	11,009
Justice, Legislation and General Government.....	2,564	4,274	4,651	8,024	7,215	12,298
Defence.....	—	—	1,331	1,627	1,331	1,627
Public Welfare.....	657	1,472	213	946	870	2,418
Education.....	1,421	2,003	—	—	1,421	2,003
Agriculture and Public Domain.....	726	951	930	990	1,656	1,941
Transportation.....	1,222	924	3,390	1,927	4,612	2,851
Subsidies to Provinces.....	—	—	3,753	4,238	—	—
Other.....	1,369 ^(b)	2	529 ^(c)	1,141 ^(d)	1,898	1,143
Total.....	7,959	11,152	20,170	28,376	24,376	35,290
Total Per Capita (Dollars).....	1.69^(d)	2.20	5.18	5.59	5.91^(d)	6.96

^(a) Compiled from the Public Accounts of the Dominion and the Provinces.

^(b) Includes a distribution of surplus to the municipalities in the Province of Ontario of \$1,361,000.

^(c) The post office revenues were netted against the post office expenditures and only the net operating deficit is included.

^(d) Excludes Ontario surplus distribution to municipalities.

While the provinces were not greatly burdened during this period by their responsibilities for public welfare, there were other significant developments which began to place a strain on their revenue structures. The most important of these was the growth of debt charges. When the debts of the provinces were taken over by the Dominion in 1867, it had been thought that the provinces would not again incur any considerable public debt. But all the provincial governments except that of Ontario had got into debt before 1896 mainly as a result of developmental expenditures of their own. The topography of Nova Scotia, New Brunswick and British Columbia led to capital expenditures on railways, roads and bridges which could not be met out of restricted current revenues, and the slow development of municipal institutions in these provinces prevented any large shifting of burdens to municipalities. The Dominion curtailed its developmental program after the building of the Canadian Pacific railway but the depression did not prevent Quebec and Manitoba from assisting railway construction. Quebec, in particular, attempted a vigorous railway and colonization policy. By 1896, its debt charges amounted to two-thirds of the debt charges of all the provinces at that date. As the weight of debt charges increased, it pressed against the confines of the revenue system.

On the other hand, Ontario took advantage of its freedom from debt charges to expand other services. With an adequate network of railways and a mature municipal system which carried

much of the cost of local roads and public works, the provincial government was able to increase considerably its assistance to education and public welfare. In the early nineties when the increased outlay on these services threatened to raise total expenditures above the yield of the existing revenue sources, the Province moved into the field of direct taxation.⁴⁵ However, for all the provinces taken together the amounts spent on education and public welfare during this period did little more than keep pace with the rise in population.

Total current expenditures of the provincial governments on transportation fell slightly between 1874 and 1896 and the only marked increase, aside from debt charges, was in the cost of the administration of justice and general government. This was due, in part, to the extension of government services to a wider area as well as to an increased population. The general government overhead varied widely as between provinces. It rose more steeply in Quebec than in Ontario and expenditures of Manitoba and British Columbia on this item more than trebled in this period. British Columbia with one-fifteenth of the population of Ontario was spending two-thirds as much as Ontario on general government and administration of justice. To a considerable extent, this disparity was due to the obstacles of topography and the lack of a developed municipal system in British Columbia.

⁴⁵ The preamble of the statute which first imposed succession duties in Ontario recited the heavy burden of expenditures for public welfare as the reason for the levy. See *Statistics of Ontario*, 1892, c. 4.

*The Provinces embark on Direct Taxation—
corporation taxes and succession duties*

In each of the seven provinces, despite the smallness of the increases in expenditure, the total requirements exceeded the yield of the revenue sources on which they had relied at the time of entering the union. Total provincial revenues from public domain doubled and those from licences and fees almost trebled between 1874 and 1896 but, in absolute terms, these additions were small. Even when supplemented by the modest increases in subsidies to some provinces, they did not suffice to meet the demands for expenditure. Before the end of the period all of the provinces had resorted to direct taxation of some kind. In 1896, corporation taxes, succession duties, property and income taxes were already providing about 10

and Prince Edward Island attempted to supplement their revenues by an income tax and, lacking a developed municipal system, both imposed provincial taxes on real property. Most of these ventures into new fields of taxation date from the early nineties, after unsuccessful demands for subsidy revision.

Behind the search for revenues lay the fact that the provincial governments had turned out to be more important agencies for collective action than the framers of the financial settlement had anticipated. Their per capita expenditures increased and their revenues from public domain did not expand sufficiently to bridge the gap. In efforts to combat the depression, they tried to push development on their own frontiers, thus incurring debts and debt charges. Failure to

TABLE 12.—GOVERNMENT REVENUES ON CURRENT ACCOUNT^(a), 1874 AND 1896

(Thousands of Dollars)

	Provinces		Dominion		Total Provinces and Dominion	
	1874	1896	1874	1896	1874	1896
Federal Subsidies.....	3,842	4,301	—	—	—	—
Taxes:						
Customs.....	1	—	14,443	19,479	14,444	19,479
Excise.....	—	—	5,617	9,170	5,617	9,170
Corporation Taxes.....	—	156	—	—	—	156
Succession Duties.....	—	428	—	—	—	428
Income Taxes on Persons.....	—	13	—	—	—	13
Taxes on Real Property.....	42	180	—	—	42	180
Taxes on Personal Property.....	—	108	—	—	—	108
Poll Taxes.....	—	65	—	—	—	65
Other Taxes.....	—	4	213	—	213	4
Sub-total.....	43	954	20,273	28,649	20,316	29,603
Licences, Permits, Fees, Fines and Penalties ^(b)	651	1,756	14	266	665	2,022
Public Domain.....	1,413	2,801	351	299	1,764	3,100
Sales of Commodities and Services.....	97	63	738	543	835	606
Other.....	619	97	225	201	844	298
Total.....	6,665	9,972	21,601	29,958	24,424	35,429

^(a) Compiled from the Public Accounts of the Dominion and the Provinces.

^(b) Including Liquor Licences.

per cent of total provincial revenues. Beginning in 1873, British Columbia pioneered the field of direct taxation, trying real and personal property taxes, poll tax and income tax as well as succession duties before the end of the period.⁴⁶ Quebec, in 1882, was the first province to attempt to levy a corporation tax, and New Brunswick followed shortly afterwards. All seven provinces were levying succession duties in 1896. British Columbia

secure a generous revision of subsidies led to a general introduction of direct taxation. This was the most significant development in public finance in this period. The movement of the provinces into the fields of corporation taxes and succession duties was later to have far-reaching and unfortunate effects upon the whole structure of Canadian public finance.

⁴⁶ Ex. 172, Brief of B.C., Pt. V, Table 124.

Summary, 1867-96

In the first thirty years of Confederation, the physical framework of the Dominion had been completed and the basic national economic policies for the future had been adopted. Despite these achievements, the period was one of trial, discouragement and even failure. The national economic expansion failed to materialize. The long depression naturally weakened the newer and more tenuous loyalties and the Federal Government which, at first, undertook its appointed task of national leadership with vigour and assurance floundered and seemed to have lost its way. Its hesitations helped to undermine its claim to dominate the provinces. Provincial loyalties, on the other hand, showed an unsuspected strength

and Privy Council decisions confirmed the provinces in possession of a large sphere of action beyond the reach of the Dominion. But the provinces were caught in a financial strait jacket from which they laboured, as yet unsuccessfully, to free themselves. The provincial governments lacked financial resources, while the Dominion failed to evoke a spirit of national loyalty. In these circumstances, it was by no means clear, at the end of the period, that the equilibrium necessary to a working federalism could be reached. It was not clear whether room could be found for the free play of provincial aspirations without denying to the Dominion the confidence and loyalty it needed for the advancement of common national purposes.

CHAPTER III

THE WHEAT BOOM, 1896-1913

1. NATIONAL ECONOMIC EXPANSION AND INTEGRATION

For twenty-five years the new nation had languished and even the most sanguine were troubled by forebodings about the success of Confederation. Then a fortuitous conjuncture of world circumstances brought with a rush the fulfilment of hopes long deferred. Life began to stir in the frame erected years earlier for a trans-continental economy. Directed by the national policies of all-Canadian railways, western settlement and protective tariffs, it grew with a rapidity surpassing all expectations. A vast and sudden transformation was wrought by the magic of wheat. The wheat boom brought a flood of settlers into the West and created two new and flourishing provinces. It precipitated a new era of railway development and spurred on the industrialization of Central Canada. Immense capital expenditures were necessary to equip the West and the growing urban and metropolitan areas of the East. Wheat worked a new integration of economic life and linked together the fortunes of the different regions.

In the optimism and prosperity of the day, the Federal Government recovered the initiative it had lost in the stagnation of preceding years and plunged again into the work of national development which the Fathers had assigned to it. The boldness and success of its new enterprises stimulated national pride. The development of the West was a national achievement and the participation of all areas in a common effort fostered a new sense of nationhood. Sons and daughters of the Maritimes and Central Canada migrated to the plains and built up the West, thus forging innumerable links between the older Canada and the new. Expansion on the distant frontier either solved or postponed the problems of provincial adjustments and regional interests. The Federal Government did not resume the attempt to dominate the provinces which had marked its earlier period of leadership and Dominion-provincial friction died almost completely away. Local and cultural diversities were partly reconciled and partly overshadowed in the dazzling success of the western development.

Success at Last—the turn in world circumstances brings a settlement boom on the Prairies

The Great Depression and the long period of economic stagnation in Canada came to an end in 1896. Prices, which had fallen 40 per cent (Statist Index) since 1870-75 began to rise. This reversal of trend was primarily due to economic factors operating throughout the entire world. The early nineties marked the beginning of a remarkable increase in the world's output of gold. During 1896-1914, as a result of the discovery of the deposits of the Transvaal and improved mining processes, world production was over three times as great as that of the eighteen preceding years and the world's stock of gold rose by 50 per cent. The absorption of this large increase in supplies by monetary systems in the days of the freely operating gold standard, and the rapid expansion of banking institutions, were important factors in the persistent and world-wide rise in prices.

The prices of raw materials, including foodstuffs, rose more rapidly than those of manufactures, especially iron and steel. This fact had immense significance for Canada. After 1896, the industrialization of Western Europe and the United States proceeded at a pace which amounted almost to a second industrial revolution. In the United Kingdom, France, Germany and the United States, the output of pig-iron and coal doubled between 1895-99 and 1910-14. The rapid growth of population, combined with the crowding of people into large industrial cities, created a rising demand for foodstuffs, particularly cereals. The full impact of this demand was felt in Canada. Hitherto the American West had been the granary for the expanding industrial population of Europe. But most of the good American lands had been taken up and it was natural that further demands for grain would push the frontier into the open plains of the Canadian Northwest.

The economic circumstances were unusually favourable. Selling prices were rising and costs were either falling or rising more slowly. Between 1896 and 1909-13, as is shown in Table 13, the average of the prices of all Canadian exports increased 32 per cent, that of grains and flour

TABLE 13.—CHANGES IN PRICE AND COST TRENDS,
1870-1913

	Percentage Decrease	Percentage Increase
	1870-75 Average to 1896	1896 to 1909-13 Average
General Level of Canadian Wholesale Prices ^(a)	- 35	+ 43
Canadian Selling Prices—		
Exports ^(b)	- 4	+ 32
Grains and Flour ^(a)	- 40	+ 32
Wheat-Liverpool	- 46	+ 33
Canadian Costs—		
Imports ^(b)	- 35	+ 24
Imports of Iron and Steel Products ^(b)	- 34	+ 6
Prices of Manufacturers ^(c)		+ 20
Ocean Freight ^(d)	- 47	+ 7
Interest Rates ^(e)	- 23	+ 28

^(a) Michell, H., "Statistics of Prices," *Statistical Contributions to Canadian Economic History* (Toronto, 1931).

^(b) Taylor, K. W., "Statistics of Foreign Trade," *Ibid.*

^(c) Dominion Bureau of Statistics.

^(d) Isserlis, L., "Tramp Shipping, Cargoes and Freight," *Journal of the Royal Statistical Society*, Part I, 1933, p. 122.

^(e) Yield on U. K. Consols.

increased 62 per cent and the price of wheat at Liverpool increased 33 per cent. On the other hand, the average of the prices of Canadian imports rose only 24 per cent and that of manufactured goods 20 per cent in the same period. A development of probably more far-reaching significance was the phenomenal decline in ocean freight rates. In 1896 ocean rates were only about half of what they had been during 1870-75 and they continued to fall until 1908, while wholesale prices were rising.

The great decline in transportation costs, the increase in the prices of cereals and the relative cheapening of the factors which entered the costs of production, i.e., manufactured goods and imports in general, suddenly brought the virgin resources of the Prairies within the scope of the international market and within the range of profitable exploitation. Capital and capital goods, the essential means for making this exploitation possible, were cheaper than ever before. The prices of iron and steel, which largely determined the cost of railways and of the implements of production, were falling steadily in relation to the values of the products of the farm. Interest rates were the lowest in recorded history and the British investor was willing to lend overseas in unprecedented volume. "At last Canada's hour had struck."

The favourable conjuncture of events after 1896 suddenly made the vast Canadian Prairie attractive to settlement. Another set of circumstances made

it available almost as soon as its attraction was felt. The comparative uniformity of conditions, the concentration on a single crop and the ease with which transportation facilities could be provided and cultivation begun in a grassland terrain, meant that practically the whole region became at once profitable and open for development. Homes did not have to be hewn out of the forest nor clearings widened by slow and tedious stages. The ready assistance of governments and the painfully acquired experience of the early settlers had by 1900 largely solved the problems of production. The spring wheat culture, fall ploughing, and summer fallowing, were the major adaptations of farming methods to the semi-arid conditions and the short growing season of the Prairies. Henceforth, the speed of development depended upon the availability of men and capital. The Federal Government threw its energies and resources into the provision of both.

All the unoccupied lands in the Northwest were under the control of the Dominion. Hence the occupation of them was directed by the national purpose of rapid and unhampered settlement. With the termination of the railway land grant system in 1896, the free homestead became the mainstay of Dominion land policy. Out of a total of about 140,000,000 acres available for settlement, nearly 60,000,000 were set aside for free homesteads. In a period of rising prices, rising land values and cheap credit, the lure of these free lands in the "last, best west" was irresistible. The vigorous immigration policy of the Dominion, the efforts of the railways and "enterprising" land companies accelerated the rush from Europe and the United States to seize the new opportunities of the Canadian Prairies. The inflow of settlers began in earnest soon after the opening of the century and during the subsequent years of the period, the land was taken up with amazing rapidity. "An area larger than Vermont was 'entered' in free homesteads in 1909; twice the area of Connecticut in 1910; more than Delaware and New Hampshire in 1911; nearly the area of Maryland in 1912; and more than Massachusetts in 1913. . . ." ¹ By the end of 1913, the rapid phase of western settlement was over. In so short a time, the frontier was pushed to its limits in almost all directions.

The occupation of the Prairie lands proceeded with little discrimination. There were no classifications of resources, no soil surveys, no climatic

¹ Chester Martin, "Dominion Lands Policy," p. 819. (Canadian Frontiers of Settlement Series, Vol. II.)

records to guide either the government or the unwary settler. The policies and methods of the Dominion were mainly designed to serve the national purpose of filling the Northwest at once with as many people as possible. The selection of land was left largely to chance and to the devices which colonization agents, railways and land companies employed in their own immediate interests. The sectional survey, the railway land grant scheme, and pre-emptions illustrate a system designed for indiscriminate mass colonization² and it worked with almost mechanical perfection. Adjustment to the vagaries and failings of nature was left to time and bitter experience.

Prior to 1908, all the odd-numbered sections over the entire Prairie region were reserved for railway land grants. The railways were allowed to select their lands in areas "fairly fit for settlement". Under this clause nearly all the grants were taken up in the brown soil zone and in the wooded country of the Park Belt.

In 1908 when the location of the grants was completed, the whole area comprising the "dry belt" (southwestern Saskatchewan and eastern Alberta) which the "land-grant railways" had avoided was thrown open for free homesteads and pre-emptions. Up to that time settlement was largely confined to the park country and the tall grass plains. After 1908, the settlers induced by the pre-emption and deceived by a period of super-normal rainfall, swarmed into the dry area.

The ranching leases in the territory long thought to be fit only for grazing were terminated and the lands put under cultivation. "Instead of warning off the homesteader from areas of submarginal agriculture, it was thought necessary to warn off the rancher from encroaching upon the range of the free homestead, and to give the homesteader right of way in case of conflict between the two."³ The flatness of the country, and the absence of forests and other obstructions facilitated extremely rapid settlement. Between 1910 and 1915, some 860 miles of railway were built south of the South Saskatchewan River. In the short space of about seven years, virtually the whole of the Dry Belt was occupied.

Whatever mistakes may have been made and resources wasted, the settlement of the Northwest was largely accomplished by 1913, and for the time being, at least, both the dry and the more humid

areas had been brought into profitable production. Between 1896 and 1913, one million people moved into the three Prairie Provinces and the population increased from 7 to 20 per cent of the total population of the Dominion. The area of occupied land increased from about 10 million acres to 70 million acres and the production of wheat from approximately 20 million bushels to 209 million bushels. At the end of the period, the value of agricultural production reached a total of \$300 to \$400 million annually.

Settlement Boom makes National Economic Policies Effective—general expansion and national economic integration

The development of the Northwest within so short a time brought prosperity and rapid economic expansion to the rest of Canada. The settlement of the Prairies took place within the framework of the national policies of all-Canadian transportation and protective tariffs. The resolute application of these policies directed the growing demands for capital equipment, for manufactured goods, for distributive and commercial services into Canadian channels, thus bringing expansion in other parts of the Dominion.

The construction of the railways, the deepening of the canals and the improvement of the harbours necessary to transport the increasing volume of Western grain over Canadian routes, stimulated economic activity in the East and gave it a large share in the moving of western products to the markets of the world. The building of towns and cities on the Prairies, the equipment of the farms and the consumption demands of the population required a large quantity of manufactured goods. The protective tariff enabled Canadian manufacturers to capture the greater share of this new market, thus giving a tremendous impetus to industrialization in Ontario and Quebec, to the coal and steel industries of Nova Scotia and to the lumber industry of British Columbia.

The two national policies of all-Canadian transportation and protective tariffs, were closely related. The former made direct economic intercourse between the separate regions possible; the latter promoted East-West traffic; and, under the stimulus of Western expansion, the two together produced a remarkable degree of interdependence among the widely scattered and diverse communities of which Canada is made up. An economically loose transcontinental area was transformed into a highly integrated national economy.

² For a discussion of this indiscriminate settlement and some of its results, see Ex. 236, Brief of the Edmonton Chamber of Commerce, pp. 19-22.

³ Chester Martin, *op. cit.*, p. 526.

All-Canadian Transportation—the great policy of national development and the foremost object of federal finance; unbounded optimism and the birth of the railway problem

The Dominion's railway policy played a significant part, both in promoting the settlement of the Northwest and in making that settlement the basis of expansion in other regions of Canada. "Railways and continually improving transportation were as essential as rain and sun to progressive settlement on the Canadian prairie."⁴ Prior to 1896, railway transportation in Western Canada was virtually controlled by the Canadian Pacific Railway. After the abandonment of the monopoly clause in the Canadian Pacific Railway charter in 1888, other lines were built and projected in southern Manitoba, principally those of the Northern Pacific; but there was little competition. In 1896, Mackenzie and Mann obtained their first railway charter and established the nucleus of that phenomenal enterprise, later to become known as the Canadian Northern. With the liberal guarantees offered by the Province of Manitoba which was ever anxious to encourage the construction of independent lines, the Canadian Northern rapidly acquired a network of railways on the Prairies. In 1902, it had 1,200 miles of line including a connection with Port Arthur.

While the relation between settlement and railway construction in Western Canada was immediate and direct, the influence of western settlement upon the transportation system in other parts of Canada was indirect but of far-reaching importance. The mounting volume of grain moving outward to the markets of the world and the increasing quantities of manufactured goods and equipment moving into the Prairies taxed the capacity of the existing facilities connecting the East with the West. This aroused the concern of the Dominion Government and inspired the imagination of railway promoters.

In the East, this growing traffic brought to the Grand Trunk its first period of real prosperity. In the West, the well-placed and economically-built lines of the Canadian Northern yielded increasing profits. Both systems were anxious to improve upon their good fortunes; the former by securing a direct connection with the western source of its expanding traffic; the latter by building a line to the East. The Dominion Government, alert to turn the commercial benefits of Prairie settlement to national advantage, was anxious to retain the

flow of Western traffic within Canadian channels. Neither company could realize its ambition without the assistance of the Dominion. The nature and extent of the assistance given ensured that the extension of railway facilities would be in accordance with the aims of national policy and not necessarily in accordance with the conditions of economical and efficient transportation. As events later proved, the optimism of the period, the political exigencies and rival ambitions of the time made these two aims incompatible.

The increasingly rapid rate of settlement after 1902 spurred both the Dominion Government and the two railway companies into action. During the railway debates of 1903, Sir Wilfrid Laurier stated the Government's policy and the necessity of carrying it out immediately:—

"... we cannot wait, because at this moment there is a transformation going on in the conditions of our national life which it would be folly to ignore and a crime to overlook; we cannot wait, because the prairies of the North-west . . . are now invaded from all sides by the white race. They came last year 100,000 and still they come in still greater numbers. Already they are at work opening the long dormant soil; already they are at work sowing, harvesting and reaping . . . We consider that it is the duty of all those who sit within these walls by the will of the people, to provide immediate means whereby the products of those new settlers may find an exit to the ocean at the least possible cost, and whereby, likewise, a market may be found in this new region for those who toil in the forests, in the fields, in the mines, in the shops of the older provinces. Such is our duty; it is immediate and imperative. . . . Heaven grant that it be not already too late; heaven grant that whilst we tarry and dispute, the trade of Canada is not deviated to other channels, and that an ever vigilant competitor does not take to himself the trade that properly belongs to those who acknowledge Canada as their native or their adopted land."⁵

In 1902, both the Canadian Northern and the Grand Trunk asked the Dominion for authority to carry out their plans to build a transcontinental railway. Attempts were made by the two companies and the Government to reach an agreement which would avoid the duplication involved in the construction of two additional lines across the continent, but they were without success. Under the prevailing optimism and political pressure, the Government did not insist and in the end gave generous assistance to both.

The original proposal of the Grand Trunk was to construct a line from Winnipeg to the Pacific Coast and then to link Eastern Canada with Winnipeg through the United States, via Chicago. When a charter for this route was refused by the Dominion, the Company proposed to build from North Bay and asked for assistance amounting

⁴ W. A. Mackintosh, *Prairie Settlement: The Geographical Setting* (Toronto, 1934), p. 44.

⁵ *Debates, House of Commons, 1903, pp. 7850-60.*

roughly to half the land and three-fifths of the cash subsidy paid to the Canadian Pacific Railway. The Government, however, feared this scheme would result in the diversion of the western traffic over the Company's lines to Portland rather than to Canadian ports. The expressed willingness of the Grand Trunk to connect with the Intercolonial was not taken seriously and the Government finally took the initiative to protect its own policy of all-Canadian transportation. The Dominion Government proposed to build a line (the National Transcontinental) from Moncton to Winnipeg and to lease it to the subsidiary of the Grand Trunk (The Grand Trunk Pacific) which was to construct a railway from Winnipeg to the Pacific Coast.

The National Transcontinental was to be located and built in accordance with the two-fold object of providing an all-rail outlet for western grain to Canadian ports and of opening "... to colonization the rich hinterland of Ontario, Quebec and New Brunswick". The agreement with the Grand Trunk Pacific in 1903 declared the purposes of the Government:—

"It is hereby declared and agreed between the parties to this agreement that the aid herein provided for is granted by the Government of Canada for the express purpose of encouraging the development of Canadian trade and the transportation of goods through Canadian channels. The Company accepts the aid on these conditions and agrees that all freight originating on the line of the railway, or its branches, not specifically routed otherwise by the shipper, shall, when destined for points in Canada, be carried entirely on Canadian territory, or between Canadian inland ports, and that the through rate on export traffic from the point of origin to the point of destination shall at no time be greater via Canadian ports than via United States ports, and that all such traffic, not specifically routed otherwise by the shipper, shall be carried to Canadian ocean ports."⁶

Private capital would not undertake the venture under the conditions imposed by the Government. In order to secure its objects of all-Canadian transportation and development, the Dominion had to provide virtually all the capital required for the entire transcontinental project. The line from Moncton to Winnipeg was to be built wholly out of government funds. From Winnipeg to the Pacific Coast three-quarters of the cost (not exceeding \$13,000 per mile in the Prairie section) was to be met by Dominion guaranteed bonds.

During 1902, the Canadian Northern obtained authority to build a railway from Port Arthur to Montreal. In 1911, when the Company was ready to go ahead with this plan, the Dominion Govern-

ment was prepared to furnish the necessary assistance. Bonds to the extent of \$35.5 million were guaranteed for a line from Port Arthur to Ottawa. The preamble to the Act providing for aid to the Company set out the aims of the Government and indicated the optimism with which still another transcontinental project was undertaken:—

"Whereas, having regard to the growth of population and the rapid development of the production and trade of that portion of Canada lying west of the Great Lakes, and to the rapidly expanding trade and commerce of Canada generally, it is in the interests of Canada as a whole that another line of railway designed to assist in the direct and economic interchange of traffic between the eastern and western portions of Canada, to open up and develop portions as yet without railroad facilities, to promote the internal and foreign trade of Canada, to develop commerce through Canadian ports, and to afford the Government system of railways in Quebec, New Brunswick, Nova Scotia and Prince Edward Island an interchange of through traffic, should be constructed from the Pacific Ocean to the city of Montreal."⁷

While the Federal Government was assuming these extensive commitments to link together the separate regions, promote national development and keep Canadian traffic flowing over Canadian routes, the provinces, particularly those in the West, were energetically securing the construction of local lines both by guarantee and direct investment. Total railway mileage increased from 18,140 in 1901 to 30,795 in 1914. During the same interval, the railway mileage in the Prairie Provinces rose from 4,141 to 11,709. In 1914 there were more miles of railway in Canada per 1,000 inhabitants than in any other country in the world. Three railway systems (at 1914, two were not quite completed) spanned the continent. There were three lines through the wilderness of Northern Ontario, three lines, two of them running side by side, through the Rocky Mountains and three connections between Central Canada and the Maritimes, two of them through Canadian territory.

The extent of these costly duplications over long stretches of unproductive country shows the optimism of Dominion railway policy and the grandiose schemes of the railway promoters which this policy supported. Whether or not this optimism was pardonable in the spacious days of 1900-13, the burdens which it ultimately imposed on the Federal Government must be regarded as the cost of promoting the national purposes of development, national economic integration and political unity. It is true that many regional, provincial and local interests were served, but only incidentally to the

⁶ *Statistics of Canada* (1903), 3 Edward VII, c. 71, sec. 42 of the agreement.

⁷ *Statistics of Canada* (1911-12), 1-2 George V, c. 6.

prosecution of larger purposes. The cost was heavy. The aid given and commitments undertaken by the Dominion Government for railways up to 1914, are set out in Table 14.

TABLE 14.—DOMINION GOVERNMENT ASSISTANCE
TO RAILWAYS
(Millions of Dollars)

	To March 31, 1914
Cash Subsidies—	
Canadian Pacific Railway System.....	48.5
Canadian Government Railways.....	3.2
Other.....	48.5
	100.2
Direct Investments on Construction and Advances—	
Canadian Pacific Railway System.....	39.7
Intercolonial and Prince Edward Island Railways.....	115.1
National Transcontinental and Quebec Bridge.....	155.0
Hudson Bay Railway.....	6.1
Other Canadian Government Railways..	13.7
Grand Trunk System.....	72.5
Canadian Northern System.....	.8
Other.....	.4
	403.3
Bonds Guaranteed—	
Grand Trunk System.....	35.0
Canadian Northern System.....	59.7
	94.7
*Total.....	598.2

* In addition the Dominion gave net land grants amounting to 31.8 million acres.

During the rising prosperity of 1900-13, these onerous burdens were not galling and, in any case, it was thought that the rapid growth of the country would quickly justify the gigantic undertakings. As long as these were still in the construction stage and the interest on the mounting railway debt was capitalized and as long as the increasing capital imports due to the building of the railways swelled the Dominion revenues, there was no strain on the public finances. Almost all of the heavy capital expenditures of the Dominion Government during 1900-14 were met from current surpluses and the net debt rose by less than \$70 million. In 1911, the Minister of Finance stated that: "Twenty years ago it would have taken six years' revenue to pay the net debt; ten years ago it would have taken five years' revenue to pay the net debt; today less than three years' revenue would pay the whole net debt of Canada".⁸ The lavish railway guarantees had not yet come home to roost, and of course it was thought they never would. It was during this period of buoyant revenues and high confidence that the Canadian railway problem was born.

⁸ Budget Speech, April 4, 1911, p. 8.

The provision of national transportation facilities was but one aspect of Dominion railway policy. To attain the objectives of that costly policy it was necessary to secure a level of rates which would counteract the North-South pull of geography and of possible alternative routes and draw traffic over the East-West lines instead. Hence the Dominion played an important part in shaping the railway rate structure (by legislation and by rulings of the Railway Committee of Privy Council and later of the Board of Railway Commissioners). The nature and extent of its intervention were fixed by its determination to encourage inter-regional traffic and all-Canadian transportation.

The objectives of the Dominion appear clearly in the Crow's Nest Pass Agreement of 1897. Under this agreement, the Canadian Pacific Railway, in return for a subsidy for the construction of the Crowsnest Pass line, undertook to reduce rates on grain and flour moving from the Prairies to the Head of the Lakes by 3 cents per 100 pounds and to reduce the rates on a considerable list of settlers' household and building supplies moving westward from Fort William and points east by 10 per cent. In the Manitoba-Canadian Northern Agreement of 1901, the Railway Company, in consideration of a provincial guarantee of its bonds and the lease of the Northern Pacific lines in Manitoba, agreed to reduce its tolls on grain from points in Manitoba to Fort William and Port Arthur by 4 cents per 100 pounds or to reduce all other rates to and from the Head of the Lakes by about 15 per cent.⁹

Following this agreement, a reduction of 2 cents per 100 pounds on grain and 7½ per cent on other freight was granted to points in Saskatchewan and Alberta. The decision of the Board of Railway Commissioners in the Western Rates Case (1914) lowered the Saskatchewan and Alberta rate scales approximately to the level of those of Manitoba. The agreement with the Grand Trunk Pacific in 1903 stipulated "that the through rate on export traffic from the point of origin to the point of destination shall at no time be greater via Canadian ports than via United States ports." The net effect of these reductions was to make Canadian grain rates the lowest in the world. While these reductions were being made in Western rates the Eastern Export Rates Case in 1905 and the International

⁹ A reduction of 2 cents per 100 pounds on grain was put into effect on February 1, 1902 and a further reduction of 2 cents on October 7, 1903. In addition, the reduction of about 15 per cent on all other freight was put into effect on June 1, 1902. This agreement was not the result of Dominion policy but the condition established by the agreement resulted in reductions elsewhere later ordered by the Board of Railway Commissioners.

Rates Case in 1907 resulted in a decrease of about 10 per cent in export rates from Ontario and in the merchandise class rates in Eastern Canada. The rates between the Maritimes and Central Canada were directly under the control of the Dominion through its operation of the Intercolonial. Because of the location of the line and the desire to promote traffic, the tolls were kept far below the level of profitable operation.¹⁰

It is impossible to relate here all the detailed effects of Dominion policy on the Canadian freight rate structure, but sufficient of the important cases have been cited to indicate their influence in the considerable lowering of rates that took place during this period. The broad decline in the level of rates was accompanied by a narrowing of regional differentials. This, together with the special concessions to certain commodities encouraged inter-regional trade and promoted the development of new areas, particularly Western Canada where the farmer was greatly benefited by the low rates on grain. The Dominion was bending the railways to its dominant purposes.

A Booming Market for Manufactures—protective tariffs direct demands of railway expansion and western settlement into Canadian channels

The third national policy which was a factor in directing the course of development during 1896-1913 was the tariff policy. Although it was inspired by other motives and originally adopted to deal with different problems, it was nevertheless closely related to the Dominion's transportation policy. The two together released a set of complementary influences which buttressed the transcontinental political union with an integrated transcontinental economy. Under the dynamic and expansive force of western settlement, these influences were effective. During the stagnation of the Great Depression, the "National Policy" tariff of 1879-87 had not produced any notable results. The disappointment gave increasing force to the complaints of the Maritimes and of the exporting industries of Central Canada. These complaints were strong enough to bring about some tariff reductions in the early nineties. However, the effect of the reductions was limited because the price decline made many specific duties increasingly protective. On the other hand, the burden of the tariff tended to decline due to the relative fall in the prices of

manufactured goods, and the great decreases in the costs of transportation.

The period of expansion which began in 1896 brought an entirely different set of conditions. The development of the West created a new and powerful interest in low tariffs while the growing demands of the settlers made the protective principle all the more desirable to the industrial East. Furthermore, a new competitive situation emerged with the rise of the United States as a great manufacturing nation. The Canadian tariff policy during 1896-1913 was a compromise between these opposing interests and also an attempt to make western development the basis of a general expansion.

The agitation for lower duties brought a significant innovation in the tariff of 1897. Instead of the almost traditional offer of a reciprocity treaty with the United States, a reciprocal clause offered a reduction in duties of one-eighth, and after July 1, 1898, one-quarter, to all countries adjudged on the whole to have given equally favourable treatment to Canada. Great Britain was immediately granted this reciprocal tariff. In 1898, the general offer of reciprocity was replaced by a British Preferential Tariff of one-fourth lower than the ordinary duties. During 1900 the differential was increased to one-third.

In 1904, an anti-dumping clause was inserted in the tariff giving added protection against extremely low-priced imports, particularly iron and steel, without a general increase in duties.

A complete revision of the Customs Tariff Act was made in 1907, introducing an Intermediate Tariff in addition to the British Preferential and General Tariffs. Apart from the establishment of these three schedules, the changes in duties were few. The uniform one-third differential in the British preference was removed and a separate preference was given for each item. The Intermediate Tariff which was approximately 10 per cent below the General was to become effective only as commercial treaties were negotiated. These general changes were the main adaptations of the Canadian tariff to the changing circumstances of the 1896-1913 period.

None of them resulted in any important alteration in the level of protection to Canadian industry. There were numerous reductions in individual items but they were made mainly at the expense of the treasury, without much modifying the degree of effective protection. In a few cases, however, considerable decreases were granted, particularly on articles entering into the cost of production of western agriculture, such as farm implements and

¹⁰ Prior to 1913 the Maritime freight rates were about 20 per cent below those of Central Canada. The first of the increases which by the end of the War (1914-18) brought the Maritime rates up to the level in Ontario and Quebec was put into effect in 1913.

tools, binder twine and barbed wire. The duties on primary iron and steel were reduced but the loss in protection was offset by increase in and extension of the bounties.

The changes in the structure of the Canadian tariff after 1896 were, in the main, attempts to placate the low tariff interest of the growing exporting industry of the West while at the same time maintaining protection against the rising competition from the United States. The strategy of national policy was to bring about an East-West economic integration, an East-West interdependence and an East-West flow of traffic over the costly transcontinental transportation system; the tariff policy was part of this strategy. In addition to other considerations, the British Preferential and the Intermediate Tariffs were devices to cheapen imports from Britain and Europe which would move over the East-West route without lowering the barriers which restricted the South-North flow from the United States. The commercial and industrial opportunities of the western development were not permitted to be seized by the "ever vigilant competitor" to the South but were reserved to "those who toil in the forests, in the fields, in the mines, in the shops of the older provinces".¹¹

Under the circumstances, the moderate degree of tariff protection was a practical compromise between the various interests concerned. The settlement of the Northwest took place with the tariff as one of the given conditions. With rising prices and rising land values, it did not impose any immediate burdens. The rapidly increasing demands for manufactured goods brought great industrial expansion in the East without the shelter of a higher level of protection. The Government pursued its announced policy of "moderation and stability", and countered the insistent demands from certain quarters for increased duties with the reply that: "The best way you can help the manufacturers of Canada is to fill up the prairie regions of Manitoba and the Northwest with a prosperous and contented people, who will be consumers of the manufactured goods of the east".¹² In the political arena, the tariff was a 'sleeping dog' that was allowed to lie. Laurier wrote to Tarte: "The question of the tariff is in good shape if no one seeks to force the issue".*

The industrial expansion of Canada after 1896 was remarkable. Between 1890 and 1910, the net

value of manufacturing production increased by nearly three times. In spite of an increase of nearly 200,000 farms in the Prairie Provinces during the period, the proportion of the total gainfully occupied engaged in manufacturing remained about the same. Although a vast agricultural region was added to the economy, the ratio of urban to total population increased from 32 to 45 per cent. While the value of agricultural production rose by leaps and bounds—the value of the exports of wheat and flour alone in 1913 was greater than the value of all exports in 1896—the value of the manufactured goods produced for the home market increased at an even faster rate.

TABLE 15.—THE NET VALUE OF PRODUCTION OF MANUFACTURES—CANADA^(a)
(Millions of Dollars)

	Totals for Establishments with Five Hands and Over	
	1900	1910
Textiles.....	32.9	67.3
Clothing.....	20.0	43.7
Wool Textiles.....	4.0	4.4
Cotton Textiles.....	6.5	13.0
Iron and Steel and their Products.....	35.0	106.3
Agricultural Implements.....	5.5	10.7
Railway Rolling Stock.....	5.2	25.2
Boilers, Tanks and Engines.....	2.8	7.6
Bridge and Structural Steel Work.....	0.7	2.8
Wire and Wire Goods.....	0.8	2.2
Primary Iron and Steel.....	3.1 ^(b)	14.9 ^(b)
Rubber Products.....	0.6	3.4
Tobacco.....	3.1	13.2
Boots and Shoes.....	7.6	13.0
Furniture.....	4.3	8.0
Liquor.....	5.3	18.7
Flour and Grist Mill Products.....	5.5	25.3
Glass Products.....	1.0	3.1
Chemicals.....	3.9	12.2
Electric Light and Power.....	2.0	12.9
Total of above Manufactures.....	106.2	286.4
All other Manufactures.....	108.3	278.1
Grand Total.....	214.5	564.5

^(a) The Census of Canada, 1901, 1911.

^(b) Excludes iron smelting.

Manufacturing expanded in most of the important categories: the provision of capital equipment, consumers' goods of general consumption and the processing of natural products for export. The program of railway construction, the growth of cities and towns, the equipping of western farms and the extension of community facilities in both East and West gave a great

¹¹ See p. 69.

¹² Budget Speech, April 16, 1903.

* January 27, 1903, O. D. Skelton, *Life and Letters of Sir Wilfrid Laurier*, Vol. II, p. 183.

impetus to the production of capital goods. The iron and steel industry particularly made rapid progress. Although imports were large, the tariff and the bounties diverted a substantial portion of the growing demand to the Canadian producer. Between 1896 and 1913, the Dominion paid nearly \$17 million in bounties. Although, during the same interval, Canadian consumption of pig iron increased tenfold, Canadian manufacturers managed to increase their share of the domestic market from 67 to 80 per cent.

The duty on steel rails (\$7 per ton), which reserved the market mainly to the domestic producer, was the principal basis of two large steel enterprises, one in Nova Scotia and the other at Sault Ste. Marie. Under the tariff of 30 per cent on cars and 35 per cent on locomotives, the production of railway rolling stock became a major secondary industry. The new demand for the equipment of western farms brought a 250 per cent increase in the output of agricultural implements. The boom in construction generated a great expansion in the production of machinery, structural steel, wire and nails.

The rapid increase in the population and the addition of a large specialized agricultural group in Western Canada greatly broadened the market for consumers' goods. The rise in the demand for such items as boots and shoes, clothing, cotton textiles, rubber goods, furniture and tobacco, was, by means of the tariff, directed very largely to Canadian sources. Between 1900 and 1910, the net value of the output of this group of products more than doubled. However, little progress was made in the production of luxury goods and articles of finer quality and imports were large. In the case of woollen textiles, linens and silks, upon which the duties were relatively low, the domestic industries lagged.

The improvements in transportation, new discoveries, increased foreign demand, and technological developments opened new opportunities for the exploitation of Canada's natural resources and in turn encouraged the growth of processing industries. Important beginnings were made in non-ferrous metal smelting and the manufacture of pulp and paper while the older saw-milling, flour-milling, meat and fish packing industries expanded considerably. Between 1896 and 1913, the exports of flour rose from \$700,000 to \$20 million, planks and boards from \$8.5 million to \$20 million, wood-pulp from \$700,000 to \$6 million and the exports of printing paper reached over \$11 million in the year ending March 31, 1914.

The settlement of the Prairies dominated the Canadian economic scene, but there were significant stirrings in the forests and mines of Northern Ontario and Quebec and British Columbia.

The most striking feature of the industrial expansion was its concentration in Ontario and Quebec. Seventy-eight per cent of the increase in the total net value of manufacturing between 1890 and 1910 occurred in these two provinces. If the production for export (lumber, wood-pulp and preserved fish), iron and steel and local industries such as baking, printing, buttermaking, are excluded, the Maritimes made very little progress. In these three Provinces, the numbers employed in manufacturing increased but there was a decline in the proportion of these to the total of gainfully occupied persons. With the cheapening of transportation and the growing advantages of large-scale production, industry was drawn nearer to the rapidly increasing populations of Western Canada and the Central Provinces, and nearer to the centre of United States' industry which financed and controlled so many of the Canadian manufacturing enterprises. The tendency toward concentration in the St. Lawrence Valley was particularly strong in the case of consumers' goods. Table 16 shows that the concentration was not only great but that in many important manufactures it was increasing during this period.

TABLE 16.—THE NET VALUE OF MANUFACTURING PRODUCTION—PERCENTAGE OF TOTAL FOR CANADA IN ONTARIO AND QUEBEC^(a)

	1890	1910
	%	%
Textiles and Textile Products.....	84	90
Clothing.....	86	95
Cotton Textiles.....	77	80
Boots and Shoes.....	88	94
Furniture.....	81	97
Tobacco.....	92	95
Rubber Products.....	98	91
Liquors.....	88	83
Glass Products.....	90	73
Chemicals and Chemical Products.....	88	75
Iron and its Products.....	85	81
Agricultural Implements.....	99	98
Hardware and Tools.....	93	92
Railway Rolling Stock.....	97	67
Wire and Wire Goods.....	91	92
Total of Industries listed.....	85	85
Grand Total Manufactures.....	81	80

^(a) Compiled from the Census of Canada, 1891 and 1911.

The manufacturing industries of the Maritimes not only failed (with the exception of iron and steel) to derive any substantial benefits from the western development but they also lost ground in their own markets. The small industries and the handicrafts which filled many of the needs of the local communities declined under the competition of the mass-produced articles of Central Canada. The processing of many household requirements moved from the self-sufficient family and the village artisan to the factories of Ontario and Quebec.

On the other hand, the iron and steel industry in Nova Scotia was directly dependent upon western settlement and the railway building and construction boom associated with it. The iron and steel tariffs and bounties enabled the Nova Scotia industry to participate extensively in the expansion. Rails and railway rolling stock were among the items of principal importance. The output of pig iron rose from 32,000 tons in 1896 to 425,000 tons in 1912, the latter constituting about one-third of the Canadian consumption. However, the rapid growth of the iron and steel industry did little more than make up for the decline in manufacturing that was experienced in certain fields.

The national transportation and tariff policies which did not produce any significant results during the Great Depression were manifestly successful under the impetus of western settlement. The wheat from the Prairies moved over Canadian railways, along Canadian waterways and partly at least through Canadian ports to foreign markets. The income from exports was spent largely on manufactured goods and equipment supplied by the Canadian producer. The steel mills and coal mines of Nova Scotia, the manufactures of Ontario and Quebec, the lumber mills and fruit farms of British Columbia were no longer restricted to the limited local demand or to the small and uncertain foreign market, but became increasingly dependent, either directly or indirectly, upon the expanding and protected market on the Prairies. The hitherto isolated and almost self-contained regions were united with an increasing volume of inter-regional trade. In the growing inter-relationships and inter-dependence, there was a common basis for prosperity and expansion.

The Inrush of Foreign Capital—its great importance in the rapid provision of capital facilities; the rising but vulnerable prosperity

The pace of economic development during 1896-1913 was made possible by a huge investment of capital. The expansion took place in the centre of a country of vast distances. It was based on the exploitation of the natural resources of an immense area. These facts, combined with the bulky character of the products and the scarcity of labour, made necessary a large physical equipment. The required capital could have been obtained at home only very slowly. One of the important factors in this rapid growth was the ease with which money could be borrowed abroad. Soon after the turn of the century, Great Britain began to lend overseas in greater volume than ever before and Canada became a favourite field for investment. In 1897, interest rates had fallen to the lowest levels in modern history and during that year the Dominion Government floated a long-term loan in London at an effective rate of 2.88 per cent compared with 4.5 per cent in 1879 and 3.25 per cent in 1888. In 1900, the securities of the Dominion Government were placed on the Trustee List in England. Throughout the period, British money was available for public and private borrowing in Canada at low cost.

The boom in investment, although comprising a wide range of industries and activities, was most marked in the field of transportation. Between 1900 and 1913, nearly \$1,400 million were invested in railways, canals and harbours. These were the main instruments of development and the necessary means for the promotion of internal trade. The policy of all-Canadian transportation greatly added to the demand for equipment. If the connections between the different regions, and from each to the seaboard had been made via the more economical routes through the United States, or via the existing railways, waterways and ports of that country, the transportation overhead on the Canadian economy would have been very much less. However, in view of the evident progress of the country and the great optimism about its future, the costs of achieving the national objectives were readily assumed. Where private credit was not sufficient, the pledging of the public credit easily brought forth the quantities of capital required.

TABLE 17.—TOTAL CAPITAL INVESTMENT IN
SELECTED INDUSTRIES
(Millions of Dollars)

	By 1900	By 1910	By 1913
Farm Buildings and Farm Working Capital.....	780	1,705	—
Capital Employed in Manufacturing.....	447	1,248	—
Mining, value of Buildings and Plant.....	43	109	—
Capital Employed in the Fisheries.....	11	17	24
Sub-total.....	1,281	3,079	—
Capital Invested in Railways.....	950	1,700	2,200
Dominion Investment in Canals.....	79	97	107
Capital Invested in Electric Railways.....	39	102	141
Sub-total.....	1,068	1,899	2,448
Total.....	2,349	4,978	—

The equipping of western agriculture in so short a time also involved a heavy investment of capital. During this period nearly 200,000 farms were established on the Prairies. All the buildings, machinery, live stock, etc., had to be newly created or brought in, and between 1901 and 1911, the value of such property increased by nearly \$500 million. While a large proportion represented the capital of immigrants and the savings of the settlers, a substantial part was borrowed from mortgage and implement companies, banks and merchants.

Although the growth of western agriculture overshadowed progress elsewhere, there were important developments in other primary industries. The spectacular but, in many cases, short-lived activities in the gold fields of the Yukon, the silver mines of Ontario and the lead-zinc-copper ventures of British Columbia, and the less dramatic but more continuous progress of coal mining in Nova Scotia and Alberta attracted considerable amounts of capital. The rising Prairie demand for lumber stimulated the saw-mill and logging enterprises of the Pacific Coast. The pre-War years also saw in Ontario and Quebec the beginnings of the hydro-electric and pulp and paper industries which require heavy investments of fixed capital.

The expansion in the production of natural products for export, the increase in population and the directing influence of the national policies promoted a rapid growth in manufacturing. Small factories supplying a limited local demand grew into mass-production establishments producing for the national market. As the demand for all kinds of manufacturing expanded, many new industries were launched. The transformation and extension

of manufacturing facilities required a large investment and between 1900 and 1910 capital employed in manufacturing increased by about \$800 million.

The growth of the industrial equipment of the country was accompanied by an equally remarkable addition to what may be called community equipment. The population was not only growing rapidly but was becoming more and more concentrated in urban centres. In the Prairie Provinces, the urban population rose from 103,000 to 469,000 in ten years; in Central Canada, the population of the leading cities doubled; and Montreal and Toronto became metropolitan centres. This growth involved large expenditures not only on buildings but also on the many facilities (roads, streets, waterworks, sewerage and electric light systems, street railways, etc.) which are necessary in urban communities. Between 1900 and 1913, municipal debts which were mainly incurred for these purposes rose from about \$100 million to nearly \$540 million.

During the fourteen years prior to the War between \$4,500 and \$5,000 million was invested in capital goods. The expenditure of this vast sum was the chief basis of the rising prosperity of the time. In striking contrast to the stagnation of the eighties and early nineties this prosperity brought economic fulfilment of the high hopes of the Confederation scheme, so sorely disappointed in the earlier period. The expanding frontier in the West and the development of internal trade under the influence of the national policies was accompanied by a great investment boom. The many political, social and economic problems engendered by the long depression found at least a temporary solution. The high rate of construction activity financed from foreign borrowings created a large demand for domestic commodities and labour. Industries formerly dependent on the export outlet found profitable markets at home. Workers in depressed areas and occupations readily obtained employment elsewhere. The surplus population of the Maritimes and of the rural counties of Ontario along with a great tide of immigrants found new homes on the Prairies and in the cities of the St. Lawrence Valley. Between 1900 and 1913, well over a million immigrants came and remained in the country; these, together with the large inflow of capital, built a greater, more prosperous, and more economically interdependent Canada. In the success of these common efforts, the foundations for a stronger political unity were laid.

By 1913, the country was equipped with magnificent capital facilities. About half of what had been added since 1900 was obtained by

borrowing abroad. These foreign obligations placed a heavy fixed charge upon the economy, the price of the rapid development that the borrowings made possible. The export capacity of the economy, which had to provide the interest due the foreign lenders, was greatly increased. Exports rose from \$156 million in 1900 to \$443 million in 1913 but in the latter year about one-third was absorbed in the payment of interest and dividends abroad. While the justification for these large commitments lay in the rapid rise in exports, the character of the latter was such that they were subject to wide fluctuations. During this period, the productive capacity of the country was tremendously enhanced but it also became more vulnerable to external influences. The economy which was so highly geared to large foreign borrowings and rising prices would encounter a severe dislocation when faced with a cessation of capital imports and falling export values.

Effect of Wheat Boom on the Regional Economies
 —Prairies the main exporting region; Ontario and Quebec the industrial and financial centre; slow progress in the Maritimes

In a few years between 1896 and 1913, the structure of the Canadian economy was basically changed. The settlement of the Prairies, the great importation of capital and the direction given by the national transportation and tariff policies transformed the isolated and depressed regions into an integrated and prosperous transcontinental economy. The most important factor in the development of the new situation was the rise of the Prairies as the important export region. This area, which in 1913 had one-fifth of Canada's population, was almost exclusively concerned with the production of wheat and its sale on the international market. Nearly 60 per cent of the gainfully occupied were directly engaged in agriculture which was dominated by this one crop. The remainder were chiefly employed in the commercial and distributive trades serving the farming community. Only about one-third of the population lived in urban centres. The large volume of wholesale and retail trade, and the financial, transportation and other services required by a highly specialized agriculture, were virtually the only support of the few cities that had rapidly grown up. Winnipeg became the Chicago of the Canadian West.

The economy rested almost completely on wheat. This one crop appeared to justify the large amount of capital borrowed abroad and invested in Western

Canada, and it was the chief justification for most of the heavy investments of foreign money in the other sections of the Dominion. The Prairie region provided the principal economic contact of the country with the external world; one-third of Canada's exports out of which the external debts would have to be serviced consisted of wheat and flour. The rise to predominance of this commodity took place during the rapid development of international trade and investment which characterized the pre-War period. The exchange of European manufactures for foodstuffs grown overseas raised standards of living and greatly extended the productive area of the world. Hoping to become the granary of Europe, Canada became deeply committed to the continuance and further development of this international economic specialization and took the heavy risks involved in so great a dependence upon a single industry.

Along with the dramatic expansion of the Prairies which focused attention during this period, new export areas began to develop in British Columbia and Northern Ontario and Quebec. The extension of the railways and technological progress made possible a significant beginning in the exploitation of the resources of the Pre-Cambrian Shield. Between 1896 and 1913, the exports of nickel and silver rose from \$2 million to \$26 million and those of pulp and paper increased from less than \$1 million to \$18 million.

In British Columbia, the production of non-ferrous metals reached \$17.1 million and exports of canned salmon \$6.6 million in 1913. However, the chief factor in the economic progress of the Pacific Coast Province was the rise of the lumber industry. The Dominion's transportation policy linked British Columbia to the Prairie market which took about 70 per cent of its lumber. While exports were important, the expansion which brought a trebling of population was heavily dependent upon the wheat boom.

On the other side of the continent, the Maritimes, although profoundly affected by what was going on elsewhere in Canada, did not share equally in the buoyant prosperity of the period. Their golden age had reached its peak with the Reciprocity Treaty and the American Civil War and its decline coincided with the achievement of Confederation. Shipbuilding, the carrying trade, the self-sufficient agriculture, the small local manufactures and the flourishing fisheries, which were the cornerstones of the economy, declined with technological changes and unfavourable circumstances in foreign markets.

During the eighties and nineties, the iron steamship all but ousted the sailing vessel from the world carrying trade. Many thought that the coming of the railway would bring new opportunities compensating for this blow to their commerce by linking a large hinterland to their ports. The Federal Government had earlier built the Intercolonial and its transportation policy later resulted in the extension of the Canadian Pacific (the "Short Line") to Saint John, and the National Transcontinental to Moncton.* However, with the higher cost of railway over ocean transport and the larger capacity of steamships, traffic was irresistibly drawn to the inland St. Lawrence ports and the great American ports to the south. Nearness to Europe which was an advantage in the days of the sailing ship was no longer so. Nevertheless, there was some progress in the development of the Maritimes, as outlets for inland commerce, and in this, federal assistance and policy played a large part. However, between 1891 and 1911 the combined population of Saint John and Halifax rose but slightly (78,000 to 89,000) and part of this growth was at the expense of the smaller outports which declined.

With the rise of grain production in the American and Canadian West and the fall in the costs of transportation, Maritime agriculture was forced to undergo a substantial readjustment. The relatively poor soil, the small fields and scattered farms could not compete with the cheap imports of grain and live stock. It became necessary to specialize in the production of crops where there was the least disadvantage, namely roots and fruits for export, and fodder for the lumber camps and the sheltered dairy industry. This specialization, however, did not permit expansion and the gainfully occupied in agriculture decreased from 134,000 in 1891 to 114,000 in 1911.

The difficulties of manufacturing in the Maritime Provinces during the period have already been described.¹³

The fisheries, Nova Scotia's most important export industry, likewise encountered unfavourable circumstances. With the development of meat packing, canning and refrigeration, the fish markets were more and more limited to the sugar islands of the Caribbean where economic conditions were depressed. The encouragement of beet sugar production by European countries greatly curbed the markets for cane sugar and thus

severely restricted the purchasing power of the West Indies. Although there was a rise of nearly 50 per cent in the general price level, the value of Nova Scotia's production of fish increased only 22 per cent between 1896 and 1913. The quantity of dried cod exported fell, and the number of men engaged in the fishing industry declined.

Throughout this period, the Maritimes were forced to undergo difficult readjustments. These readjustments had to take place within the framework of the national policies which, in some respects, hampered them and, in others, provided alternative occupations. The tariff policy imposed a drastic change in the conditions under which the Maritimes had developed. It curtailed the growth of new exporting industries and hastened the decline of the old. On the other hand, the tariff and the federal transportation policy linked these provinces with the expanding regions to the west and enabled them to share in some of the demands created by the wheat boom. The rise of the Nova Scotia steel and coal industries was directly dependent on the protective duties, steel subsidies and the great program of railway construction. On the whole, however, the forces which tied the Maritimes to the continental interior failed to induce an expansion sufficient to offset the changes which had destroyed their dependence upon the sea and weakened their relations with foreign markets. The Provinces languished and their men and capital sought opportunities elsewhere. However, by migrating to the scenes of greater opportunity many shared in the benefits of the expansion. During 1896-1913, the population of the three Provinces increased a mere 9 per cent compared with an increase of nearly 60 per cent in the rest of Canada.

At the beginning of this period, Ontario and Quebec, although sheltered by a protective tariff and connected with the Northwest by a transcontinental railway and with the Maritimes by the Intercolonial, had few relations with the rest of the country. They had their own contacts with foreign markets. The scope of their commercial and industrial activities was confined mainly to their own areas. In the early nineties, Canada's leading exports were lumber, cheese, fish, cattle and barley, and of these all but fish came chiefly from the two Central Provinces. Forest and agricultural products were the principal staples and the fluctuations in their sales in foreign markets determined the ebb and flow of prosperity. At the end of the period in 1913, this condition had entirely changed. Exports had become a relatively minor

* For fuller discussion of transportation policies in relation to the Maritimes see Book II, Section F, Ch. V.

¹³ See pp. 74-5.

factor in their economy. The Canadian, and more particularly the Prairie market for manufactured goods, transportation, commercial and financial services had become the main support of the economic life of the St. Lawrence Valley.

The western settlement and the national policies induced a rapid expansion, a great investment of capital and a measure of prosperity not experienced in the Central Provinces since the 1850's. With the highly specialized export production in Western Canada and the decline in the competitive position of the small Maritime manufacturers, Ontario and Quebec became the manufacturing centre of the country. The growing volume of traffic from the Prairie region moved over the railways, the waterways and out through the ports of the Central Provinces. The banks, insurance companies, mortgage companies and other financial institutions of these older communities quickly extended their activities to the expanding West where they came to occupy virtually the whole field. This commercial and industrial concentration was accompanied by a rapid urbanization and the growth of metropolitan centres in Central Canada. It was accompanied also by the rise of great national business organizations having their headquarters in Montreal and Toronto. Manufacturing, finance and transportation came to be dominated by a few large corporations whose operations extended across the entire continent. This period saw the development of a remarkable centralization in a country of such widely separated and varied regions.

The wheat boom had finally brought the realization of the economic objectives of the Confederation scheme. The Northwest was settled and the Federal Government was able, through its policies and projects, to ensure expansion in the older communities of Canada on the basis of that settlement. These communities, restricted by the exhaustion of their own frontiers and confined to a precarious dependence on their own foreign outlets, received a new stimulus from the highly specialized exporting industry on the Prairies which had become the country's principal economic contact with the external world. Wheat transformed the static and isolated regions into an integrated and expanding national economy. The rising prosperity which accompanied this growth in interdependence fortified the political structure of Confederation with a common material interest and a national spirit such as had never existed before.

Growth of National Unity and Rise of Canadian Nationalism—success of Dominion policy and common basis of prosperity alleviate regional and provincial discontent

In this atmosphere of large plans and their successful execution, Canadians began to believe themselves to be a great people. Their work in creating the West gave them that sense of common achievement which marks a nation. They were proud of what they had done and this gave them confidence in the future. Sir Wilfrid Laurier merely echoed a widespread conviction when he proclaimed that the twentieth century belonged to Canada.

This pride and optimism was manifested in several ways during the period. The Alaska Boundary Award was greeted in 1903 by an outburst of indignation throughout Canada. It was felt that the diplomatic bargaining of Great Britain and the United States had ignored the rights of a nation. This humiliation was a sharp reminder of Canada's dependent colonial position and it reinforced the movement for autonomy.

The autonomy movement itself was the product of a national consciousness. The desire for a privileged and sheltered position inside the Empire which had moved the colonies before Confederation was largely spent. A spirit of national exclusiveness struggled with older loyalties and with undoubted pride in the Imperial connection. The period was marked by the see-saw of these forces. Under the Laurier Government, the various proposals for closer relationships within the Empire were coolly received. Autonomy was more to be desired than Empire federation. Canada elected to establish its own navy rather than to contribute directly to a system of centralized imperial defence, and was not disposed to participate in the framing of British foreign policy. The Borden Government, after 1911, set out to modify this policy. But its naval bill was rejected by the Senate and overtures for some share in the framing of British foreign policy were coolly received by a British Government conscious of the difficulties of divided responsibility.

The growing national consciousness and confidence also contributed to the defeat of Reciprocity in 1911. For years after Confederation, both parties had attempted to secure a renewal of reciprocal trade relations with the United States. It was in despair of such a desirable arrangement that the National Policy had been adopted in 1879.

After many doubts and disappointments, the widespread prosperity of the first decade of this century appeared to vindicate the policy of industrialization by protective tariffs. The conviction that the nation could work out its own destiny, imperialist sentiment, resentment at the United States and the pressure of special interests combined to turn down Reciprocity when it was at last offered.

Nationalism had a potent influence on external relations. Internally, it worked hand in hand with other favourable circumstances to promote political harmony. Western expansion brought prosperity to the older provinces and eased regional difficulties which might otherwise have sought political expression. The bold leadership of the Federal Government seemed everywhere to be creating opportunities rather than imposing restrictions. The impressive results secured won a new respect and loyalty for federal policies.

There was no revival of the centralizing tendencies which had marked the leadership of the Federal Government in earlier days. The decisions of the Privy Council had undermined the theory of federal dominance. The Liberal Party, which was in power during 1896-1911, had recruited much of its strength from the elements which combatted the Macdonald conception of Confederation and struggled for provincial rights. Its policy was greatly influenced by the personality of Sir Wilfrid Laurier who consistently tried to promote a closer harmony between the French and English through mutual tolerance and understanding. The prevailing philosophy of Canadian federalism in this period, therefore, aimed at national unity through voluntary co-operation of an acknowledged diversity of elements. The Dominion was alert to avoid policies which would cut athwart provincial interests.

Dominion powers of reservation and disallowance were much more sparingly exercised. The power of reservation was exercised in the sole instance of a British Columbia bill relating to Oriental immigration.¹⁴ While there were 29 disallowances of provincial acts in the period, 19 of these were accounted for by the repeated enactment in British Columbia of discriminatory and restrictive measures against Orientals. The Dominion considered these to be either beyond the legislative power of the Provinces or contrary to Dominion or Imperial policies and interests. On these grounds, it was prepared to act firmly but it abandoned the earlier practice of disallowing

provincial statutes on the ground that they were inequitable, confiscatory or contrary to sound principles of legislation.¹⁵ The competence of the provincial legislatures to decide such issues was acknowledged.

The Dominion also began to consult the provinces on matters of common concern. Dominion-provincial conferences were encouraged as instruments of co-operation and through them the Dominion tried to secure a satisfactory final revision of subsidies. In face of this conciliatory attitude of the Dominion, the provinces were less inclined to be aggressive. They pressed strongly for a revision of subsidies but in the conferences of 1902, 1906 and 1913, they did not seriously criticize federal policies or demand radical constitutional changes. They were mainly concerned with their fiscal difficulties and not with fundamental adjustments in Dominion-provincial relations. The general prosperity was a powerful solvent of political as well as economic difficulties.

2. PUBLIC FINANCE, 1896-1913

Rapid Rise in Government Expenditures—extensive assistance to development, the occupation of the frontier and urbanization

Between 1896 and 1913 there was an immense growth in public expenditures. Total Dominion, provincial and municipal current outlay was multiplied four times, rising from \$63 million to \$253 million. The growth in population naturally involved additional outlay by governments but the per capita expenditures almost trebled. The forces which brought about this extraordinary jump in the costs of government were all-pervasive, exerting roughly equal pressure on all three levels, Dominion, provincial and municipal.¹

The principal causes of this multiplication of expenditures was the enormous expansion of the economy and the important role which governments played in that expansion. The rapidity of economic development in the early years of the century was only made possible by the wholehearted efforts and lavish assistance of governments. The bringing of the western wheatlands within reach of the international market in less than a decade involved large additions to transportation facilities which private enterprise could

¹⁴ *Memorandum on Dominion Power of Disallowance of Provincial Legislation*, Department of Justice, Ottawa, 1937, pp. 70-73.

¹ The Dominion raised its percentage share of the total outlay from 38 per cent in 1896 to 42 per cent in 1913, the provinces increased their share from 17 per cent to 19 per cent while the municipal share declined from 45 to 39 per cent.

¹⁴ *Memorandum on the Office of Lieutenant-Governor of a Province*, Department of Justice, Ottawa, 1937, pp. 60-61.

not have supplied so quickly, and indeed would not have dared to embark on, without public assistance.

Moreover, the general expansion generated by the wheat boom led to new developmental expenditures everywhere. The new mining areas in British Columbia and Ontario were opened up. Provincial governments began to make grants for highway development. The Federal Government gave bounties on iron, steel, lead, petroleum and imports of manila fibre in order to encourage domestic production.² Various industries were assisted by provincial subsidies and both Dominion and provincial governments allotted increasing sums to encourage and improve agricultural production.

During the boom, two new Provinces were created and two others grew to maturity in the West. In Saskatchewan and Alberta, the entire community equipment and all the physical apparatus by which governments perform their social role had to be provided almost overnight. Transportation and communication facilities, public buildings and equipment of every kind were required. The foundations and superstructure of an educational system had to be built. Towns and villages sprang up everywhere, needing a wide variety of municipal services. People in haste to realize a goodly heritage found private enterprise too slow in providing some of the services commonly left to its care in older communities and they easily agreed in asking governments to furnish them. What was true of these two Provinces was only slightly less true of the rapidly growing Provinces of Manitoba and British Columbia.

The largest increases in government activity in Eastern Canada were due to the rapid urban development of the period. The wheat boom brought great industrial expansion, particularly in Central Canada. Towns grew into industrial cities and cities into metropolitan areas. As people were drawn from the farms and villages to the cities and towns, the problems of urban crowding required a large extension of public services. Streets and street railways, gas and electric systems, sewage systems, water supplies, schools, hospitals, libraries, etc. were required. The greater the concentration of population, the greater is the number of services which can be supplied most economically in a collective manner. Also, in the case of some services, concentration brings a rapid rise in per capita costs. This tendency

toward a geometric rather than a simple arithmetic progression of government expenditures in growing urban and metropolitan areas was an important factor in the increase in municipal expenditures in the period under review.

Finances of the Dominion—booming customs revenues spur on aggressive program of development; the lavish assumption of railway commitments

In the Confederation scheme, one of the principal functions of the Federal Government was to be the promotion of economic development, and for two brief periods (1867-1874 and 1879-84) it confidently undertook this task. Then the Great Depression dried up its revenues and sapped its initiative. When prosperity reappeared at the end of the century, the Dominion became once more the chief instrument of new and larger programs of development. With expanding revenues, its operations gained a new magnitude and sweep surpassing all its previous efforts. Doubts as to its capacity to play the role intended for it suddenly vanished.

The development of the West was under way by the beginning of the century and Canada was attracting large quantities of foreign capital. As this capital poured into the country in the form of goods, the familiar public revenue cycle of the Dominion was repeated but on a scale hitherto unknown.³ Customs, and later excise, receipts from which it drew over 90 per cent of its revenue shot upward, and as early as 1900 produced a surplus of \$8 million on ordinary account. With two or three exceptions, the Dominion piled up surpluses of increasing size each year throughout the remainder of the period. In 1912-13, despite considerable capital expenditures charged to current account, the surplus was nearly double the total gross revenues of the Dominion in 1896.

At the same time, the rapid increase of population and low interest rates were reducing the per capita burden of debt charges. In 1914, the per capita interest charges were slightly less than they had been in 1875, despite the addition of \$393 million to the direct public debt of the Dominion. Such facts make it easier to understand the boundless optimism of the time and the assurance with which the Federal Government increased its expenditures and piled up contingent liabilities. As long as the expansion continued, past commitments appeared trivial in the face of mounting

² For figures showing amounts expended on bounties in this period, see Canada Year Book, 1916, pp. 459-61.

³ In the first decade of the century the value of imports rose from \$190 million to \$420 million.

revenues and surpluses. As the conditions which would bring expansion to a halt were nowhere apparent, the dire predictions of the cautious and the timid seemed ludicrous and the unfolding of events throughout the period reinforced this superficial judgment.

Between 1896 and 1913 the current expenditures of the Dominion were multiplied four times. Expenditures on developmental projects accounted for over half the total increase. The promotion of western settlement and general expansion by lavish outlays on transportation and public domain were the principal concern of Dominion finance. It is not necessary to recount the well-known history of the liabilities incurred for the National

extension of the occupied area and the rise in salaries and wages. The Dominion undertook no new services of importance. It assumed no responsibilities and gave no assistance to the provinces for public welfare and indeed no need for this appeared. Development, particularly the railway program, overshadowed all the other functions of the Dominion.

The enormous additional burdens which the Federal Government assumed in connection with development were not onerous in the days of rapidly expanding revenues. The full weight of them was not felt until the contingent liabilities arising out of the railway guarantees became hard realities and the operating deficits of the insolvent

TABLE 18.—GOVERNMENT EXPENDITURES ON CURRENT ACCOUNT,^(a) 1896 AND 1913
(Thousands of Dollars)

	Provinces		Dominion		Total Provinces ^(b) and Dominion	
	1896	1913	1896	1913	1896	1913
Net Debt Charges.....	1,526	2,304	9,483	12,213	11,009	15,081
Defence.....	—	—	1,627	13,781	1,627	13,781
Public Welfare.....	1,472	4,343	946	2,617	2,418	6,960
Education.....	2,003	9,600	—	215	2,003	9,815
Agriculture and Public Domain.....	951	7,434	990	10,985	1,941	18,403
Transportation.....	924	8,631	1,927	35,467	2,851	41,964
Subsidies to Provinces.....	—	—	4,238	11,280	—	—
General Expenditures—Justice, Legislation, General Government and Miscellaneous.....	4,276	15,069	9,165	31,736	13,441	46,805
TOTAL.....	11,152	47,381	28,376	118,294	35,290	152,809
Total per Capita (Dollars).....	2.27	6.22	5.59	15.50	6.96	20.02

^(a) Source: The Public Accounts of the Provinces and the Dominion and the Public Accounts Inquiry of the Royal Commission on Dominion-Provincial Relations.

^(b) Inter-governmental transactions eliminated.

Transcontinental, the Grand Trunk Pacific and the Canadian Northern. In 1913, virtually the whole of the direct and indirect debt of the Dominion, amounting to \$521 million, had been incurred for railways, canals, harbours and river improvements.

Aside from development, the only significant increase in expenditure was for defence, the cost of which, due to uneasiness in Europe, rose from \$2 million to almost \$14 million. The creation of two new Provinces in 1905 and the general revision of subsidies in 1907 added some \$7 million to the federal subsidies. The outlay on general government and administration rose by over three times due mainly to the increase in population, the rapid

railways were saddled on the Dominion at a time when revenues were falling. In this period, the seeds of a perennial public finance problem were sown.

Finances of the Provinces—pre-occupation with development; the rapid increase in debts and expenditures of the Western Provinces

Between 1896 and 1913, the per capita current expenditures of the provinces increased nearly three times, their per capita debts nearly four times. At Confederation the provinces were vested with important functions but their financial

responsibilities were not great. Their revenues were narrowly restricted and it was not thought they would again incur any substantial debts. However under the circumstances of the wheat boom they rapidly enhanced their role as agencies for collective expenditures. By 1913, the total debts of the provinces were more than half, and their current expenditures nearly half those of the Dominion. The provinces had evolved from a relatively minor to an important position in Canadian public finance.

As in the case of the Dominion, the dominant factor in the rise of debts and expenditures was the pre-occupation with economic development. While the Dominion was spending lavishly to promote expansion on a national scale, the provinces were encouraging the construction of railways and facilitating settlement on their own frontiers. In 1913, 80 per cent of the total provincial debts and 40 per cent of the current expenditures were incurred for development.

The largest outlays for development were naturally made on the frontiers of the expansion, namely the four Western Provinces. In 1913 the average per capita debt of these Provinces was nearly six times as great as that of the rest of the country. In the same year, Alberta, British Columbia and Manitoba each had larger total liabilities than the Province of Ontario. Three-fifths of the western provincial debt had arisen out of expenditures on railways or consisted of guarantees of railway obligations. The latter included some \$85 million of bond guarantees granted to hasten the construction of branch lines by the Grand Trunk Pacific and of the mainline and branches of the Canadian Northern. The Prairie Provinces had also incurred considerable debts for the provision of general community facilities. In many instances it was thought that private enterprise was too slow, and that the rich natural heritage might well be mortgaged to encourage rapid settlement and to lighten the rigours of the pioneer life with a few common amenities. All of the three Provinces established provincial telephone systems. Manitoba and Saskatchewan made investments in grain elevators. Public buildings, court-houses, normal schools, universities, hospitals, roads, etc., had to be supplied almost overnight. These would fill not only the needs of the present but also those of a much greater future. Hence it was felt that they should not wait until they could be paid for out of current revenues. At 1913, the per capita debt incurred for public buildings, institutions and roads by the

Western Provinces was four and a half times as large as that in Eastern Canada.

In addition to the provision of capital facilities the Western Provinces were spending appreciable amounts on development out of current revenues. Debt charges however were still small since the railway guarantees did not as yet have to be implemented. Later, most of these were assumed by the Dominion. British Columbia, heavily dependent upon lumbering and mining, was making large outlays on public domain. Manitoba, Saskatchewan and British Columbia were already spending considerable amounts on highways. The last Province, with its difficult topography and its policy of meeting capital costs out of current revenue, was spending nearly twice as much on roads and bridges as all the other Canadian provinces combined.

The developmental programs of the Eastern Provinces were relatively on a much smaller scale than those in the West; nevertheless they were important and almost wholly accounted for the two-fold increase in their per capita debts between 1896 and 1913. New Brunswick and Quebec expended considerable amounts in extending railways to their undeveloped frontiers. Ontario built the Temiskaming and Northern Ontario Railway, guaranteed \$7.9 million of Canadian Northern Ontario railway bonds and launched the Hydro-Electric Power scheme. The Maritime Provinces concentrated mainly on the construction of roads and bridges which was responsible for the major portion of the increase in their debts. Net debt charges however did not rise substantially. Quebec which had fallen into serious difficulties in the eighties was wary of again assuming such burdensome liabilities and its per capita debt, thanks to current surpluses, actually declined during this period. The debt of Ontario was still completely self-supporting. The current expenditures on public domain and agriculture however bulked relatively large in Ontario and Quebec where the northern resources were beginning to become valuable. Nearly one-fourth of the current outlay of the Maritimes was expended on roads and bridges.

Aside from the concentration of public resources on development, there were no important changes in provincial expenditures during this period. In 1913, legislation, justice and general administration constituted 32 per cent of the total current outlay, education 20 per cent, and public welfare but 9 per cent. The average per capita cost of general government for all provinces was slightly more

than doubled. Salaries and wages had risen, the society had become more complicated and the regulatory and administrative functions had increased. The greatest rise had taken place in the Prairie Provinces and British Columbia where the per capita expenditures on general government overhead were respectively three and six times those of the Eastern Provinces. The lag in municipal development, the thin scattering of population and the rapidity with which government services had to be provided added greatly to costs. Education also called for larger outlays. The economy was becoming more specialized and the provinces responded to meet the more exacting requirements by fostering more complete and better standards of instruction. However, during the great expansion and prosperity of the time, most of the problems of social welfare, which have since become crushing responsibilities of the provincial governments, found their solution inside the private economy. The growth of specialization and urban concentration were rapidly breaking down the former self-sufficiency of households and local communities but the social implications of this change were almost unnoticed in this period of spacious opportunity for all. Added costs of public welfare were mainly due to improved care for limited classes of unfortunates.

The Rise of Municipal Expenditures—rapid urbanization in the East, and the establishment of new cities and towns in the West

Total municipal expenditures during this period rose in three dimensions. First, there was the growth in population and the establishment of many new cities and towns, particularly in the West; second, the growing concentration of the population in large urban centres with their heavier per capita costs of providing the same services; third, the extension in the variety of collective services which accompanies the increasing size of urban centres.

One of the striking social changes of this period was the crowding of people into towns and cities. By 1911, over 45 per cent of the population was classed as urban. One-third of the population lived in cities and towns of over 5,000 and almost one-fifth in cities of over 50,000. The general decline in self-sufficiency and the industrial expansion stimulated by the wheat boom and the national policies brought a sharp increase in urbanization.

The self-sufficiency of the farm household and the village community, which had marked Canadian life throughout the nineteenth century, largely disappeared with the rapid development of a specialized exchange economy in this period. Higher prices for agricultural produce led the farmer to specialize and concentrate his efforts on a few products. Improvements in transportation wiped out the "natural shelter" under which the village craftsman had flourished. These factors, combined with improvements in manufacturing technique, enabled the farmer to exchange more of his specialized products advantageously for his various requirements which were processed or manufactured in urban centres. The assembling of farm and other natural products for distant markets and the distribution of manufactured goods for farm and village consumption required an intricate financial and commercial mechanism which concentrated in a few great cities. The rapid centralization of control in industry, commerce and finance in the period speeded up this development.

Urban concentration involves large additions to municipal services and, with a rising standard of living, it leads to collective provision of many comforts and conveniences. The cost of fire and police protection, health services and education, streets and sewers increases in a much higher ratio than the numbers of the population. Urban municipalities undertake water, light, power and transportation services. The skills required in a complex specialized society can only be secured through a more expensive educational system. The amenities of parks, libraries, recreation centres, free bathing facilities, among other things, are demanded. In the result, a greater proportion of the urban income is spent on collective services which add to municipal costs but, on balance, need not decrease and may even increase the real income of the community.

Municipal expenditures and debts, as in the case of the provincial governments, rose most steeply in the Western Provinces and for much the same reasons. Between 1901 and 1911 the urban population of the West grew from 193,000 to 673,000, a rate of increase six times as great as that in Eastern Canada. The speed with which services and facilities had to be provided added substantially to the costs. In addition many western municipalities undertook ambitious schemes which far exceeded existing requirements and were based on the most optimistic estimates of the growth in population. Per capita municipal expenditures in the Prairie Provinces and British Columbia were

approximately double those of Central Canada.⁵ The Maritimes were the least urbanized region in the Dominion and the provincial governments bore a relatively higher share of the total costs of education and roads, particularly in the rural areas where municipal organization had made little headway. These factors, together with the slow increase in population, held down the total per capita outlay of local governments to about half that in Ontario and Quebec.

The rapidly rising municipal expenditures in Central and Western Canada were financed without difficulty in this period. Almost all municipal revenues were derived from a direct tax on real property. The pre-War boom was marked by a steep and sustained increase in land values which easily carried the mounting burden of taxation.

Expansion of Provincial Revenues—inelastic federal subsidies intensify development of provincial revenue sources; the growing importance of taxation

The provincial governments could not have added to their expenditures as they did between 1896 and 1913 without access to more fruitful revenue sources. The fact that they were exploring the possibilities of the unpopular direct taxes in the early nineties testified to the tightness of their fiscal positions at the opening of this period. They continued to be more or less cramped for nearly a decade after 1896. Dominion revenues improved at once with rising customs receipts. It was almost ten years before the expansion and rising capital importations permeated the economy sufficiently to affect substantially the provincial sources of revenue. During the first few years of the century, therefore, the provinces pressed for a substantial revision of subsidies.

The Provinces of Alberta and Saskatchewan which came into existence in 1905 were given the advantage of previous revisions and liberal interpretations of the subsidy formula and the sums they received showed a considerable change in the conception of provincial responsibilities. Each was given a subsidy in excess of \$1 million of which \$375,000 was in lieu of the public lands retained by the Dominion. The 80 cent per capita subsidy was to be calculated on the actual population increase until a population of 800,000 was reached in each case.

Meanwhile, the older provinces continued their agitation and the Provincial Conference of 1906 was called to effect a final revision of subsidies. The settlement, which was accepted by all governments except British Columbia, added about \$2.3 million (an increase of about one-third) immediately to the total annual subsidies paid to the nine provinces and provided for automatic increases with the rise in population.

About the time that the subsidy revision was under discussion, however, the boom began to have a marked effect on the sources of revenue on which the provinces had relied in the past with such disappointing results. Accelerating business activity boosted the income from licences and fees. Expansion of lumbering and mining brought a sharp increase in the revenues from public domain. As rising prosperity quickened the accumulation of wealth, succession duties began to bring in considerable sums. As corporate organization spread rapidly, the corporation tax became fruitful. This buoyancy temporarily relieved the financial strains of the provinces but when the boom broke they were once more in difficulties. Manitoba and Prince Edward Island got a further increase in federal grants in 1912 and at the Inter-Provincial Conference in 1913 the provinces again urged a general revision of subsidies.

TABLE 16A.—PER CAPITA MUNICIPAL GOVERNMENT EXPENDITURES, CURRENT ACCOUNT⁶, 1913

	Total Canada	Prince Edward Island	Nova Scotia	New Brun- swick	Quebec	Ontario	Manitoba	Sackst- chewan	Alberta	British Columbia
	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$
Net Debt Charges.....	2.39	0.27	0.98	0.66	2.15	2.28	3.67	2.73	5.12	6.67
Public Welfare.....	1.97	0.05	0.87	0.59	0.92	0.81	2.38	0.89	1.16	2.89
Education.....	3.04	0.99	2.14	1.69	2.43	4.29	4.68	4.66	7.33	3.44
Transportation.....	1.88	0.26	0.61	0.79	1.59	1.97	1.76	2.79	2.89	4.47
General Expenditures—Justice, Legislation, General Government and Miscellaneous.....	3.95	0.31	1.23	1.14	3.83	3.73	7.62	6.57	4.63	9.03
TOTAL.....	13.18	1.88	5.82	4.90	9.92	13.04	20.01	17.64	21.09	26.56

⁶ Source: Public Accounts Inquiry of the Royal Commission on Dominion-Provincial Relations.

By the end of this period, federal subsidies had become a relatively minor part of total provincial revenues, namely 23 per cent, compared with 43 per cent in 1896 and 58 per cent in 1874. At the same time, the proportion of federal revenues thus transferred to the provinces had dropped by one-half.⁶ On a number of occasions the provinces had suggested a formula which they hoped would keep the subsidies more in line with their growing expenditures and enable them to reap some of the benefits of the expanding revenues of the Dominion.

this resolution would be acted upon, disappeared when less than nine months later Canada was plunged into the Great War.

Federal subsidies provided less than one-fourth of the increase in provincial revenues (\$35 million) during this period. The sources from which the provinces were originally expected to meet expanding requirements, namely, licences, fees, etc., and public domain, took care of only about one-half of the increase in their needs; the remainder, \$3.4 million, was obtained from direct taxation.

TABLE 19.—GOVERNMENT REVENUES ON CURRENT ACCOUNT,^(a) 1896 AND 1913
(Thousands of Dollars)

	Provinces		Dominion		Total Provinces ^(b) and Dominion	
	1896	1913	1896	1913	1896	1913
Federal Subsidies.....	4,301	12,851	—	—	—	—
Taxes—						
Customs Import Duties.....	—	—	19,479	104,691	19,479	104,691
Excise Duties.....	—	—	9,170	21,452	9,170	21,452
Corporation Taxes.....	156	3,490	—	—	156	3,490
Succession Duties.....	428	3,611	—	—	428	3,611
Income Taxes on Persons.....	13	119	—	—	13	119
Real Property Taxes.....	180	1,753	—	—	180	1,753
Other Taxes.....	177	347	—	1,335	177	1,682
Sub-Total—Taxes.....	954	9,320	28,649	127,478	29,603	136,798
Motor vehicles, automobile licences, etc.....	—	470	—	—	—	470
All other Licences, Permits and Fees, Fines and Penalties..	1,756	6,678	266	1,516	2,022	8,194
Public Domain.....	2,801	11,046	299	3,420	3,100	14,466
Liquor Control.....	—	2,248	—	—	—	2,248
Sale of Commodities and Services.....	63	815	543	1,513	606	2,328
Other.....	97	1,507	201	1,276	298	2,392
TOTAL.....	9,972	44,935	29,958	135,203	35,629	166,896

^(a) Source: The Public Accounts of the Provinces and the Dominion and the Public Accounts Inquiry of the Royal Commission on Dominion-Provincial Relations.

^(b) Inter-governmental transactions eliminated.

The proposal that a part or all of the subsidies should consist of a constant ratio of the Dominion's receipts from customs and excise, which was advocated in Parliament in 1884 and at the Inter-Provincial Conference in 1902, came up again at the Conference in 1913. This time a formal resolution was passed asking the Dominion to give the provinces an extra grant "equal to 10 per cent of the Customs and Excise Duties collected . . . from year to year". Whatever likelihood existed that

As the expenditures rose, the disparities in the ability or ease with which the various provinces and regions could meet them became more conspicuous. Also, in the provinces where the expansion was most rapid, the population was more willing and more able to bear heavier taxes for the purpose of encouraging further development and of providing collective services which private enterprise was slow to undertake.

Next to federal subsidies, public domain was the largest single source of total provincial revenues and here the disparities between provinces were

⁶ Between 1874 and 1913, the percentage of provincial subsidies to the Dominion's revenues fell from 18 to 9 per cent.

particularly great. The Prairie Provinces did not have control over their natural resources but received a small annual subsidy from the Dominion in lieu of them. In British Columbia, where lumbering and mining were the principal activities and where the expenditures on public domain were large, the revenues therefrom were ten times as great per capita as in the Eastern Provinces. The other traditional method of raising provincial revenue, i.e., the imposition of licences, fees, etc., was used most intensively in the Prairie Provinces where, after federal subsidies, it constituted the main source of income. In the Maritimes the receipts from this item were almost negligible.

The largest reserves of provincial revenue lay in the power of direct taxation. The growing demands upon expenditures and the inelasticity of federal subsidies forced the provinces to make more and more use of such taxes despite their unpopularity. The extent to which they were levied in each of the provinces depended upon the nature of the economy and the magnitude of the total outlay. In British Columbia where the level of expenditures on a per capita basis was many times as high as in the other provinces, the per capita receipts from taxation were nearly six times those in the rest of the country. While British Columbia had a highly developed system of taxation, including taxes on personal incomes, real and personal property, the levies in the other provinces were confined almost exclusively to corporation taxes and succession duties.⁷ The two latter imposts were most productive in Ontario and Quebec. The industrial and commercial expansion stimulated by the wheat boom and the national economic policies was accompanied by a rapid concentration of corporate activity and of large private fortunes in Central Canada. The receipts from corporation taxes and succession duties, therefore, rose steeply and by 1913 yielded 26 per cent of the total provincial revenues compared with but 9 per cent in the Prairie Provinces and 8 per cent in the Maritimes. The per capita revenue from succession duties in Ontario and Quebec was twice as high as the average of the other provinces.

A number of significant changes in the financial position of the provinces from that intended at Confederation, had already begun to emerge at the opening of this period. The demands and opportunities of the wheat boom, and the growing specialization and interdependence of society greatly

accelerated this development. Despite the cramping financial settlement of 1867, the provinces became in fact much more than large municipalities. When other revenues became insufficient, they entered the field of direct taxation which in 1913 was already producing over one-fifth of the total revenues. However, the implications of large uncontrollable expenditures and heavy debts, of the great inequalities in taxable capacity, and of the attempt to use what are in reality national taxes for provincial purposes, were not yet evident.

Summary—1896-1913

The common efforts of all regions in building up the country between 1896 and 1913 cemented the political union of 1867 and Canadians became conscious of themselves as a nation. The growing sense of community was accompanied by increasing economic interdependence. The national policies of all-Canadian transportation and protective tariffs were effective in making the wheat boom the basis of a general economic expansion in which the manufacturing industry of Eastern Canada became heavily dependent on the agricultural export region of the Prairies. With the exception of the Maritimes, which were affected by but did not share generally in the expansion, the wheat boom brought prosperity to the whole country but it was prosperity which remained conditional on the profitable production of wheat. A high degree of economic integration had been achieved but it required a sustained world demand for wheat to make it a lasting success.

As Canadians on the prairies specialized in growing wheat for the international market and Canadians in the older parts of Canada specialized in providing a wide variety of goods and services for the national market, the old self-sufficiency of pioneer days passed from the scene. By 1913, the open frontier had almost disappeared. With the coming of a highly specialized interdependence, the capacity of individuals to overcome economic reverses and mischances by their own efforts was greatly impaired and the material conditions which force governments into costly expenditures for social security were begun. With intensive industrial development came the shift from the country to the cities, bringing in its train a greater demand and a greater need for collective provision of various services.

The general expansion was accompanied by the multiplication of the expenditures at all levels of government. In part, this was due to the growth of population and the extension of the area

⁷ At 1913, British Columbia and Prince Edward Island were the only provinces levying personal income taxes. However, in the latter Province the tax was more in the nature of a tax on real and personal property than a true income tax.

requiring governmental services. In part, it was due to the undertaking of many collective services by urban municipalities. Despite these factors, the traditional preoccupation of British North American governments with economic development continued to dominate public finance and reached its greatest intensity during this period. Federal and provincial

governments spent lavishly to open the doors of opportunity for private enterprise. In so doing, they encouraged the growth of a new economy, more productive and diversified but also more vulnerable in times of adversity. Its tribulations at a later date were to alter the character as well as the emphasis of Canadian public finance.

CHAPTER IV

THE WAR PERIOD 1914-21

Introduction—the general economic, political and social effects of the War

One of the immediate effects of the War upon Canada was to provide relief from accumulating economic difficulties. By 1914 the investment boom based on foreign borrowing had come to an end. It then became imperative to turn from the construction of capital works to greater production of exportable products in order to pay the interest on the large investments of the preceding decade. This major shift and readjustment threatened to be painful and prolonged, but under the stimulus of war demands the Canadian economy turned the corner with ease and expanded its production immensely in a very short period of time. By force of circumstances, Canada's foreign borrowings dwindled until they disappeared in 1917. In the later years of the War, the great expansion in production combined with the policies of the Federal Government enabled Canada to become an important lender, financing British purchases of Canadian goods.

In addition to stimulating expansion, the War gave the Federal Government a decisive role in directing the employment of the country's resources. Canada's war effort involved a massive concentration—in many respects, a consecration—of manpower and resources for a single over-riding purpose. The Dominion Government interpreted this purpose and co-ordinated the efforts of the country. It was the appropriate agency for driving towards this single objective, but in so doing it exhibited elements of a totalitarian technique inseparable from modern war. General enthusiasm for the Allied cause produced a remarkable unanimity among Canadians of all regions and classes in the early days of the conflict. Supported by this unique expression of national unity the Government threw all its power and authority into the prosecution of the War, and as the struggle deepened it redoubled its efforts and commitments. Its vigorous policies hastened and intensified the expansion of production which was made profitable by altered world conditions. The development of the economy as well as the occupations and interests of the people were directed, and considerably distorted, by the demands imposed upon the country by the War.

The first flush of enthusiasm waned as the War dragged on and became a trial of collective endurance and capacity for sacrifice. Lacking the tremendous unifying influence of a direct and immediate threat of foreign invasion, Canadians began to differ radically on the means best calculated to reach the results desired by all. This difference about means threatened the effective pursuit of ends and broke the party truce which marked the early years of the War. During the later years, the effects of the economic and financial policies, which the Federal Government had adopted to facilitate the maximum war effort, permeated the social structure with unexpected and unfortunate results. The economic cost of prosecuting the War pressed more and more unevenly on particular groups. The contrast presented by the beneficiaries of inflation and war prosperity caused hot resentment. The inevitable and appalling inequality of burdens and sacrifices involved in modern war became manifest.

The War provided at least a partial solution of the economic problems which faced Canada in 1914 but replaced them with political and social problems of a very disturbing kind. Prolonged concentration on the single purpose of winning the War put severe strains on political unity. The "conscription issue" and its aftermath ruptured both federal political parties. The War was a great strain on Dominion statesmen and it burdened the Dominion treasury with an enormous debt. Old sectional cleavages were revived and deepened and immediately after the conflict Canada was disrupted for the first time by class conflict. In the minds of many, the conduct of the War had denied and disproved the basic community of interest upon which federal initiative and leadership must always rest. The war effort of the Dominion was magnificent but it was at the price of temporary exhaustion and serious internal antagonisms.

In Canada, as in other countries, the War had revolutionary effects. Economically, there was a vast increase in productive capacity and a rapid development toward economic maturity. But the most profound changes were broadly social in character. A society which prided itself on equality of opportunity found itself being divided into

classes. The inequality of burdens and benefits arising out of the War promoted stratification. On the one hand, large government borrowings from the proceeds of war prosperity created a rentier class while, on the other hand, class consciousness appeared in the growing industrial population harassed by the steep rise in the cost of living. Their distress led to demands for government intervention. The success with which the Dominion Government had organized a peaceful society for combat showed how governments could alter the conditions of economic and social life. If governments could organize so effectively for destruction, they should be able to organize the conditions of the good life for their citizens. Under the pressure of social inequalities which became more and more evident, this changing philosophy of the appropriate sphere of state activity led straight to extensive government intervention in economic life and to the provision and further extension of a variety of social services. As will appear later, post-War intervention came mainly from the provinces.

From Wheat Boom to War Boom—major depression averted; Canada pays for War by swift rise in export production

The extravagant boom which attended the opening of the western wheatlands broke in 1913. It had been based on the inflow of foreign capital which financed a huge program of construction. This foreign capital was attracted by the confidence that wheat could be profitably grown for export on the Canadian prairies. In 1912, interest rates rose sharply in the London money market and, in 1913, the general price level, including the prices of Canadian exports, began to fall. The stream of capital imports which fed the growing prosperity of the country was checked. The prospects for profitable production of wheat became less rosy. The boom, which had been prolific of frantic real estate speculations, optimistic corporate mergers, and many rash enterprises of a public and private nature, suddenly collapsed.

The Canadian economy was at once faced with severe difficulties. It had been geared to a high rate of investment and construction. Between 1913 and 1914, the value of construction contracts awarded fell 37 per cent. Much of the labour and resources employed in the building of railways, harbours and canals, factories and rapidly growing towns, became idle. The slackening of construction brought a sharp curtailment in the Nova Scotia iron and steel industry, unemployment in the industrial cities of Central Canada and a steep decline in the production of lumber in British

Columbia. The fall in export prices was aggravated by drought on the Prairies which cut short the crop of 1914. Caught between decreasing capital imports and falling export values, the economy which the wheat boom had brought into existence revealed its alarming vulnerability to external influences.

Adjustment to this situation required the diversion of idle labour and resources into the exporting industries to obtain employment and also to enable the country to meet the interest charges on its large external debt. Under normal conditions, this process would have been slow and painful involving a deflation of costs and prices and at least a temporary decline in industrial activity—the principal elements of a major depression. The first effects of the War were to intensify the adverse external influences and to deepen the depression which was settling down upon the country. The dislocation of normal international intercourse cut Canadian exports still further. The inflow of foreign capital came almost to a standstill because borrowings in London were being permitted only for war purposes. Unemployment was widespread in the winter of 1914-15.

After the middle of 1915, however, the dislocation of international economic intercourse became a great advantage to Canada. Britain and her Allies required vast quantities of supplies. The high cost of shipping and the readiness of the United States and Canada to supply credits directed a large part of the demand to North America. The principal requirements were foodstuffs and munitions. The former was Canada's main export and the production of the latter was quickly undertaken by the depressed manufacturing industry. From 1915 to 1918, the intensity of the demand grew ever greater and Canadian production reached new heights. The capital equipment built up during the wheat boom displayed a remarkable productive capacity and the labour force which built it was absorbed, either in the overseas forces or in the production of goods and services.

The insistent demand for foodstuffs brought a swift rise in the price level of Canadian exports. The prices of agricultural exports, in particular, rose much more rapidly than those of imports and of manufactured goods. As in the pre-War period, this gave an immediate and powerful incentive to the expansion of agricultural production. In the period between 1913 and 1919, the absolute increase in the area devoted to field crops was equivalent to the total increase which took place in the twenty years prior to 1913. In the

Prairie Provinces the acreage under wheat in 1919 was almost 80 per cent greater than it had been in 1913. In this short period, the number of cattle on Canadian farms increased by one-third. A wide variety of farm products received a less vigorous but nevertheless pronounced stimulus from the demands created by the War.

This expansion in the productive capacity of agriculture provided very substantial increases in the surplus available for export. The bumper wheat crop of 1915 with its record yields per acre and its large export surplus was the principal factor in attaining a favourable balance of merchandise trade and did much to extricate the economy from the doldrums of the two preceding years. Although the wheat yields during the remainder of the war period were disappointing and in 1918 and 1919 extremely poor, the average value of exports of wheat and flour during the 1917-19 period was more than double that of 1913.

While wheat was by far the most important export, the exports of other agricultural commodities showed even greater proportionate increases. Between 1913 and 1918, the exports of meat rose in value from \$6 million to almost \$85 million, live stock from \$10 million to \$35 million, and cheese from \$19 million to \$35 million. The exports of hay, oats, butter and eggs expanded greatly. Except where afflicted by drought, agriculture prospered. The increase in the value of its exports during 1914-19 over the immediate pre-war level was equivalent to fully four-fifths of the total Canadian money cost of the War.

Among other raw materials affected, non-ferrous metals enjoyed a sharp increase in demand. Despite progress in the development of mining, the problems of treating low-grade and complex ore-bodies had not been satisfactorily solved prior to the War. The high prices due to the War encouraged ingenuity in the search for methods of extracting the metals from these ores. Several important refining processes were discovered. High prices made the working of low-grade deposits profitable. Between 1913 and 1918, the quantity of copper produced rose 54 per cent, lead 36 per cent, nickel 86 per cent and zinc from a negligible quantity to 35 million pounds in 1918. The value of the output of these four metals rose from \$29 million in 1913 to \$74 million in 1918. This stimulus advanced the Canadian mining industry. The high prices disappeared after the War but the growth of interest in mining, the improved techniques, and the greater resources accumulated by mining com-

panies out of profits were permanent gains to the industry.

On the other hand, the lumber industry made little headway. The decline in construction and the high cost of ocean shipping bore unfavourably upon it, and production fell off. It was not until a demand arose for wooden ships and for sitka spruce in the airplane industry toward the end of the War that the industry in the Maritimes and British Columbia received any special stimulus. Circumstances only indirectly connected with the War did, however, give a great impetus to the pulp and paper branch of the forest industry. The United States tariff had been removed before 1914 and the relative exhaustion of the forest resources of the United States, the exclusion of Scandinavian supplies due to the circumstances of the War, and the war-time growth in the circulation and size of newspapers gave the Canadian newsprint industry its opportunity. The exports of pulp and paper rose from \$19 million in 1913 to \$105 million in 1919.

There was an even greater rise in the output of manufactures. The favourable influences, derived from the national economic policies, which had brought about a rapid growth of the manufacturing industry during the wheat boom, were continued by the war-time expansion of western agriculture and the increases in the tariff in 1915 (7½ per cent in the General and Intermediate schedules and 5 per cent in the British Preferential). The disruption of imports from Central Europe, the decline in British exports, and the high cost of ocean shipping enabled domestic industry to secure a larger share of the home market. The increase in production of commodities of general consumption between 1915 and 1918 is indicated by the 10 per cent increase in employment in the textile, boot and shoe, tobacco, and furniture industries.

While the growing share of the domestic producer in the home market was a feature of the period, the greatest stimulus to manufactures came from British orders for munitions and war equipment. The decline in construction and the depression prevailing in 1914 had severely affected the manufacturing industry, particularly iron and steel. Immediately after the War opened, Canadian industrialists, whose plants were idle or operating below capacity, began to press for British munitions orders. From late 1914 to 1917, these orders were given in increasing volume until exports of shells and explosives rose to almost \$390 million

in 1917. In the years 1916, 1917 and 1918, munitions made up about one-quarter of total exports and, for a considerable time, Canadian manufacturers were producing between one-quarter and one-third of the artillery ammunition being currently used by the British armies. Approximately a billion dollars worth of shells and explosives were shipped overseas and Canada supplied the Allies with ships and airplanes valued at more than \$100 million. At the peak, about one-third of the Canadian manufacturing capacity was employed on war orders from other countries. Between 1915 and 1918, the total employment in manufacturing rose by 32 per cent. The iron and steel industry which had been hit very severely by the depression in 1914, reached a new record in volume of output.

Thus, during 1914-18, there was a remarkable expansion in the total production of goods and services. It was this increase in production which paid for the cost of the War. It also met the interest charges on the external debt which could no longer be financed by further foreign borrowings, and made possible (in contrast to European countries) the maintenance of a relatively high standard of living. Under the circumstances, this was the only way the War could be financed. A society which cannot borrow abroad and employ foreign industry to produce the material sinews of war is obliged to pay for its war expenditures out of the current production of its own economy. During 1914-18 Canada was unable to borrow abroad in any significant volume¹ and the country, taken as a whole, was compelled to pay for the War as it went along.² Table 20 shows the nature and extent of the extraordinary rise in exports.

TABLE 20.—MERCHANDISE EXPORTS

Millions of Dollars

Fiscal Years	Products of the Mine	Fish	Products of the Forest	Products of Agriculture	Manufactures		Misc.	Total
					Munitions	Other		
1913.....	57.4	16.3	43.3	194.9	—	43.7	0.2	355.
1914.....	59.0	20.6	42.8	251.5	0.3	57.2	0.3	431.6
1915.....	51.7	19.7	42.7	239.1	0.5	85.0	0.7	439.4
1916.....	66.4	22.4	51.3	352.8	81.0	161.0	6.7	741.6
1917.....	85.6	24.9	55.9	501.3	281.2	196.2	6.4	1,151.4
1918.....	73.8	32.6	51.9	740.4	386.3	250.5	4.5	1,540.0
1919.....	77.5	37.1	70.5	469.7	250.9	304.5	5.2	1,216.4
1920.....	62.3	42.3	105.3	624.4	12.1	391.0	2.1	1,239.5

¹ For total Federal Government borrowings abroad during the War period, see p. 103.

² For further discussion of the means which made this possible, see pp. 99, 100.

In a very short period of time, the Canadian economy was delivered from a heavy dependence upon capital imports and showed its capacity to produce a large surplus of goods to be shipped abroad for war purposes and to provide, in this way, during the last two years of the War, sizeable capital exports. This quick transformation was not wrought by magic. Goods and services had to be diverted from the usual channels of investment and consumption to meet the requirements of the War. This large diversion was mainly accomplished by the financial and economic policies which the Federal Government was able to carry through. The character and effect of these policies determined the nature and extent of Canada's participation in the War and also, in a great measure, the impact which the War was to make on the political, social and economic structure of the country. To understand these policies and account for the vigour with which they were applied, it is first necessary to recall the political atmosphere created in Canada by the War in Europe.

1. THE WAR AND NATIONAL UNITY

A United Nation Enters the Conflict—War efforts evoke a strong spirit of unity and nationalism

There is no need to emphasize the unanimity of conviction with which Canada threw itself into the struggle. It is true that, from the very beginning, there was a latent difference of opinion as to whether Canada was involved as a principal and committed to the totality of its powers. But as no one had at that time any conception of the colossal scale of the struggle and the sacrifices it would entail, this difference was passed over and did not emerge for discussion until the later years when it was driven into the open by the logic of events. Citizens of all occupations, political persuasions and religious beliefs pronounced the cause to be just and Canada's participation unquestionably necessary. Even one as openly critical of British imperial policy as Henri Bourassa declared that it was "Canada's national duty to contribute, within the bounds of her strength and by the means which are proper to herself, to the triumph, and especially to the endurance, of the combined efforts of France and England."³

Canada had never before seen such a demonstration of national unity. For some time, the solidarity of national sentiment was the dominant feature of Canadian life. Personal interests were

³ *Le Devoir*, Sept. 8, 1914; quoted by Elizabeth Armstrong in *The Crisis of Quebec, 1914-18*, p. 78.

subordinated to the demands of a united effort and, for the great majority of people, the winning of the War became the prime objective of national existence. The evidence of a single national purpose was unmistakable and sufficed to give to the Federal Government immense moral authority in keeping with its sweeping legal powers.

The crisis brought a truce in party strife which was maintained, in essentials, for over two years and which enabled the Parliament elected in 1911 to prolong its life (with the approval of the Imperial Parliament) until the fall of 1917. In the Special Session of Parliament in August, 1914, the War Measures Bill which gave sweeping emergency powers to the Government was quickly and unanimously enacted. The Opposition did not entirely give up the right to criticize the Government, as its strictures upon war contracts, fiscal policy and the conduct of the Department of Militia and Defence showed, but frankly partisan obstruction disappeared.

Although the party truce broke down in later years, the spirit which enforced it in the early years was strong enough to bring about the formation of the Union Government in 1917.

The crisis also imposed a truce on Dominion-provincial contention. In 1912 and 1913 the provinces had again begun to demand further increases in subsidies. With the coming of the War and its great financial responsibilities for the Dominion, this claim went into abeyance. So also did the federal power of disallowance which was used on only one occasion during this period. Provincial political leaders did not challenge the drastic policies pursued or the far-reaching powers exercised by the Dominion during the War. On the contrary, they played a large part in the formation of the Union Government. Family bickering was stilled in the presence of larger issues. Provincial politics and provincial interests were overshadowed by the magnitude of the common national purpose. The efforts of the Dominion absorbed the attention of the people and commanded for the time, at least, the overwhelming support of public sentiment. Despite the range of the activities of the Federal Government and the degree to which its actions affected the lives of the people in every part of the Dominion, there was no organized or systematic protest by the provinces. When protest came, it came in the sphere of federal politics, out of the discontent of cultural, class and sectional interests and not through provincial governments. For a time, Canada exhibited the essential features of a unitary state.

The conscious nationalism which accounted for the temporary eclipse of provincialism made itself felt in external relations. It disposed the Dominion Government to regard Canada's participation in the War as that of a principal combatant and not merely as that of a satellite of Great Britain. The Canadian Army Corps was maintained as a separate unit in the field and was ultimately commanded by a Canadian. In 1916, the establishment of a Ministry of Overseas Military Forces in London brought the Canadian troops directly under the control of the Dominion Government. Where independence of action was not possible, the Dominion bid for a share of control in centralized effort. The Imperial War Cabinet provided, in an indirect but substantial way, for participation of the Dominions in the direction of the War and the Imperial War Conference of 1917 recognized "the right of the Dominions and India to an adequate voice in foreign policy", to be made effective through machinery for consultation and concerted action. After the Armistice, when the urgency for unified effort declined, the stress shifted to autonomy. While the all-absorbing sense of national unity did not survive the War, some elements of the conscious nationalism evoked by it retained their strength. With Canada leading in the demand, the Dominions got separate representation at the Peace Conference and in the League of Nations. And however much the Dominion Government may have receded from leadership in internal affairs in the post-War period, it found sufficient support for vigorous pursuit of Dominion status.

The Conscription Issue—the disruption of national unity, the political isolation of Quebec, the unfortunate effects on Canadian federalism

It was generally agreed at the outset that it would be a short war and that there was no doubt about its conclusion. The first plans for military participation involved only the sending of a single contingent of 25,000 men. It gradually dawned upon people that there was no assurance of an early decision and the military contribution was repeatedly increased until, at the beginning of 1916, the Government announced the desirability of raising the overseas forces to half a million men. The struggle became one of the endurance of peoples, as well as of armies, with all their material and spiritual resources engaged in it. Food supplies, munitions and every kind of materials became as vital to the success of the conflict as soldiers. The Government directed the production

and arranged the financing of supplies for the Allies on a great scale. By 1917, it was reluctantly seen that even the issue was in doubt and that an Allied victory could only be ensured by a supreme effort. It also became clear that the Federal Government saw Canada's most vital interests at stake in the struggle and that there were no reservations or limitations on its willingness to pledge Canada for the sake of victory.

As the Federal Government called for greater effort and sacrifice in pursuit of this supreme objective, the vague differences of opinion about Canada's relation to the struggle became practical questions. Was it engaged as one of the principal combatants or merely as a voluntary helper of Great Britain? If engaged as a principal to the full extent of its powers, in what way could the country make the most effective contribution to the common cause of the Allies? Differences of opinion always exist as to the means of reaching an agreed objective. Because there was no overpowering sense of immediate peril such as is raised by foreign invasion or the direct threat of it, many people were not readily convinced of the urgency to subordinate differences to the prime necessity of united action. As the commitments became deeper month by month, public discussion of and dissent from the policies of the Federal Government became inevitable. The practical issue upon which these differences of opinion began to widen into cleavages over policy was the question of the extent of the military contribution which Canada ought to make.

Discussion of conscription and other issues which were so disturbing to national unity over twenty years ago is a delicate matter even at this late date. But the political issues of the war period left so enduring a mark upon the Canadian federal system that they cannot be ignored. At the risk of being misunderstood we have, therefore, felt it imperative that these issues should be recalled and set out as objectively and fairly as possible.

Before conscription became a burning political question, there had been marked differences in the ratio of enlistments among the different elements of the population. Naturally enough, the response of the British-born had far exceeded that of the native-born. In the early stages, recruiting had been particularly brisk in the towns, although it fell off when the great increase in industrial activity created conditions of full employment. It was never so marked in the countryside which lacked contact with military traditions and never felt the organized social pressure for enlistment which operated in the towns. These factors which

affected the rate of recruiting in all areas of Canada might be expected to manifest themselves in a more pronounced way in the Province of Quebec.

There was a difference between English-speaking Canada as a whole and French-speaking Canada in the response to voluntary recruiting. There has been much controversy as to whether any significant difference existed after the adjustments necessary to provide fairly comparable conditions are made. In answer to reproaches made against Quebec, it has been maintained that if allowance is made for the much higher proportion of British-born in the English-speaking parts of Canada and for the predominance of rural conditions in Quebec—conditions which materially affected the rate of recruiting in English-speaking areas—the response of native-born Canadians did not differ significantly in Quebec from the rest of Canada. On the other hand, the validity of this explanation has been denied. Data to test these contentions are not available and probably can never be secured.

Even if there were marked differences, not to be explained by making these adjustments, it need not cause surprise. There were several immediate and some underlying factors making for difference. Among the official spokesmen of the Dominion Government in Quebec were men who had fought with Bourassa against Laurier and the Naval Bill and they could scarcely be expected to rouse enthusiasm for a vigorous war policy. There were serious and exasperating mistakes in the management of recruiting in the Province, mainly through lack of sympathetic appreciation of how a sensitive people cherished their distinctiveness.

There were basic factors which lay much deeper. The French-speaking Canadians had been established in Canada for centuries. They were the oldest Canadians of European stock and they were much more firmly rooted in North America than their English-speaking fellow-citizens. Their political connection with France had been severed 150 years before and they had never formed a close sentimental attachment for republican France with its anti-clerical associations. Their undoubted loyalty to Great Britain was a reasoned rather than an instinctive loyalty. It lacked the emotional pull which was essential to command deep sacrifices in a remote European war. While the rest of Canada was deeply affected by living or remembered links with the British Isles and by United Empire Loyalist and Imperial tradition, their experience and memories were essentially North American. It was not unlikely, therefore, that the attitude of the French-speaking Canadians toward a prolonged

war in Europe would differ from that which prevailed in the rest of Canada.

Before the War, Ontario had limited the use of French, both as a language of instruction and a subject of study, in the schools of the Province. French-speaking people of Ontario had vigorously resisted the enforcement of this regulation. They contested its constitutionality and the case dragged through the courts until its validity was finally upheld in 1916. In that year, Ontario enacted further legislation in support of its separate school policy and the Federal Government declined to disallow it. The dispute over the bilingual school question, as it was called, went on with increasing bitterness, revealing the gaps which divided French-speaking citizens, in feelings and interests, from English-speaking Canada and emphasizing again the difficulty of tolerable accommodation between the two races. On the instance of Sir Wilfrid Laurier, a resolution was introduced in Parliament deploring the action of the Ontario Legislature.*

The Conservatives of Quebec with Nationalist tendencies joined the Liberals from that Province in voting for the resolution; the Western Liberals voted against it and it required the full exercise of Sir Wilfrid's prestige and authority to hold the Ontario Liberals in line. The disruptive potentialities of the old racial issue even in face of the national emergency were clearly shown. The split over the bilingual question foreshadowed the much more serious division on the issue of conscription. The principle of the political co-operation of the two races in the two federal parties had already begun to break down in 1916, because one of the races was being rapidly consolidated behind one of the political parties.

The dispute over the separate school policy of Ontario embittered the debate on conscription. The French-speaking Canadians of Quebec were deeply roused by the action of Ontario. Their language was one of their most vital interests. The majority of the political leaders in Quebec strove to prevent the bilingual issue from diminishing Quebec's support of Canada's war effort. But the issue led many into bitter opposition of Canada's participation in the War. They insisted that the English-speaking leaders of the Dominion were sacrificing the real interests of Canada to British Imperialism. They maintained that no further sacrifices for the preservation of British civilization in Europe should be made at a time when a British attack was being made on the culture of French Canada at home.

The Nationalist agitation in Quebec aroused both extremist and moderate groups in other parts of Canada. It was assumed that the Nationalists spoke for Quebec as a whole and Nationalist propaganda was cited as the reason for the lower ratio of enlistments in Quebec. These charges of disloyalty, which multiplied rapidly, caused resentment among the French-speaking Canadians who had supported participation in the War and provoked recriminations which, in turn, drew further retort from English-speaking Canadians. It was a vicious circle in which mutual misunderstanding and mutual reproach seemed to be endless. When this stage was reached, it inevitably diminished the support which Quebec gave to the supreme objective of the Federal Government. The bilingual issue loosed a chain of consequences which helped to prepare Quebec for united resistance to conscription.

Quebec was not alone in its opposition to conscription. Organized labour and agriculture, by this time alarmed and burdened by rising prices and roused by the glaring inequality in the distribution of war profits, raised their voices against it. Late in 1916, the Government established a National Service Board to take an inventory of man-power. Despite disclaimers by the Government, this scheme was widely regarded as a precursor of conscription. The Trades and Labor Congress recorded its disapproval of both national service registration and conscription. Some spokesmen for agriculture lashed out at profiteers and demanded that any census or conscription of men should be accompanied by similar treatment of wealth. This demand was reiterated in the public debate on the conscription issue itself.

At the time the policy of conscription was announced, the Government was urging the maximum effort at food production. As the reserves of agricultural labour were depleted, the Government made repeated promises of liberal exemptions from military service to farmers' sons. These promises did something to calm the agitation in rural Ontario against the introduction of conscription. But cancellation of these exemptions in the spring of 1918, owing to the unexpected and desperate situation on the Western Front, brought an immediate and determined protest. A huge deputation of Ontario and Quebec farmers made a profitless visit to the Government at Ottawa and returned home angry and resentful at what it regarded as a breach of faith by the Government.

When the Government announced that conscription would be imposed, trades and labour councils

*The resolution was actually introduced by Mr. Lapointe and is commonly known as the "Lapointe resolution".

across the country voted resolutions condemning the conscription of men and demanding the conscription of wealth. Although the annual convention of the Trades and Labor Congress in 1917 gave qualified approval to the conscription policy of the Government, it significantly gave its blessing to a resolution approving the formation of a labour party for political purposes. In its view, the interests of labour were failing to find expression in the Federal Government's interpretation of the supreme national purpose.

In Quebec, the proposal of conscription met with general opposition. Popular agitation against it throughout the Province deepened into mass demonstrations in Montreal in the closing days of August, 1917. Within Parliament itself, the issue revealed to the full its disruptive force. It completed the disintegration of the federal political parties. Among Liberals from the English-speaking provinces, devotion to their old party leader was overborne by what was conceived to be the inexorable demands of the War, and close friends and personal lieutenants of Sir Wilfrid spoke and voted for the military service bill. On the other hand, the erstwhile Quebec Nationalist supporters of the Government voted against the measure. Within the walls of Parliament, the Liberal Party was becoming identified with the Province of Quebec and Parliament itself was dividing on racial lines.

Despite passionate opposition the policy of conscription commanded the support of a majority of the people of Canada. They accepted it as vital to the supreme national objective of winning the War. The most critical phase of the struggle which was reached in 1917, combined with the serious threat of internal dissension, led to a closing of the ranks. Although the idea of a coalition for the purposes of the War was not new, the conscription issue brought the agitation for a union government to a head. The existing Government had no mandate to introduce it and a drastic measure certain to arouse resistance could not very well be enforced except by a national non-partisan government.

With several leading Liberals sharing in the initiative, the Union Government was formed and the ensuing election was fought on its interpretation of the means necessary to make the greatest possible contribution to the Allied cause. During the election campaign, racial passion reached a climax of bitterness. In the result, the Union Government swept English-speaking Canada while Quebec gave solid support to Sir Wilfrid Laurier's

opposition to conscription. Out of the 143 candidates elected who were endorsed by Union Government, all but three were returned in English-speaking Canada; 60 out of the total of 77 elected candidates endorsed by Sir Wilfrid Laurier were elected in Quebec. However, the popular vote was not so one-sided. The Liberal Opposition (excluding all the minor parties and independents) received about 42 per cent of the total civil vote. Outside of Quebec the Government elected 82 per cent of the members with 82 per cent of the total civil and military vote; the balance was split between the Liberal Opposition and a scattered number of independents, many of whom supported the Government on the conscription issue.

TABLE 21.—VOTES CAST IN THE 1917 FEDERAL GENERAL ELECTION⁽¹⁾

(Thousands)

	For Candidates Officially Endorsed by Union Government	For Candidates Officially Endorsed by Sir Wilfrid Laurier	All Other
Civil Vote—			
Quebec—Urban ⁽²⁾	38	106	7
—Rural ⁽²⁾	24	232	19
Other Canada—			
—Urban ⁽²⁾	351	156	62
—Rural ⁽²⁾	496	306	110
Total Civil Vote.....	909	800	198
Military Vote.....	215	14	5
TOTAL.....	1,124	814	203

⁽¹⁾ The potential vote in constituencies where acclamations occurred was estimated on the basis of results in other provincial constituencies.

⁽²⁾ Urban-rural division only approximate.

The long standing quarrel between the Nationalists and the Liberals in Quebec was healed at last. The old Liberal Party was shattered in Parliament⁵ and in Quebec it became temporarily identified with the racial interests of the majority in that Province.

In the breakdown of old party lines, new political movements began to appear. Labour hastily constructed a political organization and ran a number of candidates, many of whom were opposed to conscription. The various farmers' movements took no separate part in the campaign. However,

⁵ It was the organization and leadership of the Liberal Party that suffered most. As later events showed, there was no permanent disaffection of its rank and file supporters.

resentment at the manner in which the Military Service Act was applied in the following year gave an impetus to political action by farmers' organizations and immediately after the close of the War they took advantage of the confusion and weakness in the Liberal Party to enter the political field.

Canadians are reluctant to recall the events which reopened old antagonisms and renewed distrust and bitterness between the two races. It is imperative that the distrust and the bitterness should be forgotten but it has been necessary to recall the events which provoked them because they have had a deep influence on the subsequent history of Canadian federalism and because they point to certain general lessons about the operation of the federal system in Canada.

The united effort required of a nation by modern war places a great strain on the political unity of any people. But the events of the Great War provide the most striking illustration of the peculiar character and the limitations of the Canadian political system. The War gave predominance to the Federal Government and set a single objective for all Canadians. In a sense, the War was a great national enterprise, a corporate endeavour by the whole country. The instinctive diversity of Canadian life did not long remain constant to a single conception of ends and means. Compromise and co-operation broke down into dissension, and coercion was resorted to as the only means of driving on to the chosen objective.

It must be emphasized again that collective action through the agency of democratic government implies a common purpose and an agreed method of achieving it. If the common endeavour is one with respect to which deep impulses in the community arouse differing conceptions, it is likely to break down and the consequent disharmony will embarrass all the common enterprises which have been entrusted to the government. A population of common origin and traditions, deeply habituated to think alike on fundamental issues, may be readily able to maintain the agreement necessary for collective action affecting the whole range of community life. Canada lacks that homogeneity and this, in turn, limits the extent of collective endeavour which can be effectively organized under Dominion control.

This is why Canada is a federal state and must remain so. Deep underlying differences cannot be permanently overcome by coercion. There are, of course, many matters in which there is sufficient

community of interest and purpose for them to be entrusted to the Federal Government and they are increasing. Modern transportation and communication and the integration of the economy lift many matters to the level of general interests which might, if agreed upon, be cared for by the Federal Government.

The illumination thrown upon the federal system by the events of the War period strengthened tendencies and opinions already evident in Quebec. To those who believed in the largest possible powers for the provinces, it seemed to confirm the policy which had commended itself to them in the past. Here was a demonstration that where the interests and ideals of French-speaking and English-speaking Canadians did not run side by side the federal powers were at the disposal of the majority. The importance to them of section 92 as a protection to their institutions and cherished values was thereby increased. Because government action is always laden with unforeseen and unexpected result, Quebec became still further disposed to question any increase in federal power.

Although this view was not universally accepted in Quebec, its influence reinforced earlier tendencies and gave Quebec a deeper distrust of federal power. Quebec became, more than before, a watchful guardian of provincial rights. In this way, the political experience of the War has had a pervasive influence on the subsequent history of Dominion-provincial relations. In other ways too, it has had far-reaching results. In its calamitous effect upon the federal political parties, it seriously damaged federal initiative in internal affairs in the post-War period and thus added to the political strength of the provinces without increasing their financial resources.

2. THE WAR AND THE CANADIAN ECONOMY

War Finance—war costs met by internal borrowing; loan funds made available by inflationary credit policy

It has already been remarked that the political unanimity with which Canada greeted the War enabled and even compelled the Dominion Government to embark on a vigorous use of the constitutional powers of the Dominion in directing the war effort.⁶ The pledge of Canadian lives was backed by the pledge of Canadian

⁶ The War Measures Act of 1914 authorized it to employ a wide range of powers, many of which were beyond its peace-time constitutional capacity.

economic resources. To ensure the most effective use of these resources, the Dominion Government employed the powers at its command throughout the war period. Through the use of them, it launched and enforced a number of economic and financial policies which governed the public finance operations of the Dominion during this period and enabled the country to become a great source of essential supplies for the Allies. These policies also had a profound permanent effect upon the economic and social structure. Therefore, they must be considered in some detail.

The outbreak of the War found Canada in a deepening depression. The financial upheaval and uncertainty further aggravated the situation. The large current surpluses of the previous years had disappeared. The Government was faced with the necessity of obtaining large loans to complete its capital program and to meet the huge war expenditures which loomed ahead. Abroad the money markets were virtually closed; a run on the banks threatened at home.

The exigencies of the War at once forced the Federal Government into an aggressive role. Early in August, 1914, the redemption of Dominion notes in gold was suspended, bank notes were made legal tender, the banks were permitted to use the excess circulation privilege⁷ the year round and finally the Government was empowered to make advances of Dominion notes to the banks upon the pledge of approved securities. While these measures averted the immediate danger to the banks, they also provided the mechanism for inflation. The restrictions thus abolished and the devices set up provided the machinery for an expansive credit system and placed it at the disposal of the Federal Government.

The financial requirements of the Dominion for the fiscal year 1914-15 were met in various ways. The customs duties on coffee, liquors, sugar and tobacco were raised and special excise taxes were imposed on liquors and tobacco. These increases in taxation, however, were expected to yield only \$15 million. Approximately \$156 million (\$61 million for War, \$93 million for capital and \$2 million current deficit) were required in addition to the total current revenues for the year. It was not thought advisable or possible to pay for the whole cost of the War out of taxation or borrowings at home. Arrangements were made with the Imperial Government to finance the Canadian cost

of the War and in the fiscal year 1914-15 almost the entire borrowings needed for the purpose were obtained from that source. The capital expenditures were met by \$40 million of loans in London, a \$39 million fiduciary issue of Dominion notes⁸ and a short term loan from the Bank of Montreal. The early period of the War thus occasioned no immediate strain on the economy. Aside from the issues of Dominion notes and a small amount of temporary loans, the whole of the war cost and the capital disbursements were borrowed abroad.

Early in 1915, the first special war taxes were imposed. Taxes were placed on bank note circulation, on the gross income of loan and trust companies, on the premium income of life insurance companies, on telegraph and cable messages, on railway and steamship tickets and on sleeping and parlour car accommodation. Postage rates were increased and stamp taxes placed on cheques, bills of exchange, etc. Imposts were made on patent medicines, perfumery and non-sparkling wines. An additional 7½ per cent was levied on imports under the General and Intermediate tariff schedules and 5 per cent on items under the British Preference. These taxation increases which were expected to yield about \$25 million went, however, only a small way toward meeting the Government's financial needs of \$166 million during the fiscal year 1915-16.

The arrangement with the Imperial Government to finance the Canadian costs of the War broke down in the summer of 1915 when sterling exchange went to a large discount. Henceforth Great Britain could do no more than finance the Canadian war expenditures made overseas. The Federal Government was faced with the necessity of itself raising the money for its war costs incurred at home and for making advances to Great Britain to meet an increasing share of the British war purchases in Canada, if these purchases were not to be sharply curtailed. With the London money market closed, New York was the only other possible source of foreign funds. A loan of \$45 million was obtained there in July, 1915. For the remainder of its requirements, the Government was obliged to turn to the Canadian investor.

Before the War, the Federal Government had never raised as much as \$5 million in Canada by way of a long term loan. In 1914, less than \$700,000 of the entire federal debt was payable in

⁷ Hitherto the banks had been permitted to issue their notes in excess of their combined paid-up capital and rest or reserve funds up to 15 per cent during the crop moving season from September to February inclusive.

⁸ The amount of Dominion notes that could be issued against a 25 per cent reserve of gold was increased from \$30 million to \$50 million, \$16 million of Dominion notes were issued against guaranteed railway securities and \$10 million were issued for general government purposes.

Canada. However, the remarkably large crop and the war orders of Britain and her Allies had brought a return of prosperity by the autumn of 1915. With the low level of private investment and the expanding profits induced by the rising price level, there was a considerable accumulation of funds. The domestic loan offered in November, 1915, produced \$100 million subscribed almost wholly by financial institutions and other business organizations.

During 1915-18, Canada's war effort was rapidly increased. The growing burden had more and more to be supported by Canada's own resources. The Imperial Government provided the funds for the war expenditures overseas. The Canadian Government paid the costs incurred at home and made advances to Great Britain for a considerable part of her purchases in the Dominion. During the last two years of the War, the Canadian advances to Great Britain (including those made by Canadian banks) far exceeded those of Great Britain to Canada. Canada was, in effect, buying a large part of her own exports and shipping them abroad where they paid for the cost of the War. The extent of Canada's contribution to the conflict, therefore, depended upon the ability of the Federal Government to obtain money to finance the exports. The more money it could raise at home, the more exports and production could increase and the more extensively the country could engage in the struggle. Three methods were available to the Government for the acquisition of funds: taxation, borrowing, and the issue of Dominion notes. Although special war taxes were imposed they produced but a relatively small part of the amount required. The issue of Dominion notes could be used only to a limited extent. The bulk of the funds had to come from borrowings.

The amount of money which was obtainable by means of domestic loans depended upon the savings of the community and the extent to which private investment was reduced. As ordinary savings became insufficient, the Government adopted the only policies then open to it, which had the effect of both increasing and of redistributing the national money income in a manner which gave a larger portion to business organizations and wealthy individuals whose profits or surpluses could be borrowed in large amounts by the Government. This expansion and redistribution of money income was brought about by the expansion of bank credit, i.e., inflation. Prices and the cost of living (selling prices) rose more rapidly than average wage rates

and interest on old debts (costs).⁹ The profits of industry and property incomes, therefore, increased while the real income of wage earners and individuals receiving interest payments at fixed rates, declined or rose less rapidly. It was this relative, and in some cases absolute, reduction in the real income of one section of the community, and the creation of large surpluses in the hands of another (which would lend these surpluses to the Government) combined with the great increase in gross production that made the surprisingly large war loans possible.

During the fiscal year 1916-17, the Canadian war expenditures rose to \$307 million. Ordinary capital expenditures absorbed another \$82 million. In that year the Federal Government required nearly \$400 million in funds. To increase the revenue from taxation and to reduce the net profits derived from war activity, a business profits tax, retroactive to the beginning of the War, was imposed early in 1916. One-fourth of all net profits (except in life insurance and agriculture) in excess of 7 per cent on the paid-up capital of incorporated enterprises and in excess of 10 per cent on the paid-up capital of unincorporated enterprises was taken in taxes by the Government. Businesses with a paid-up capital of less than \$50,000 were exempt, excepting those engaged in the production of war supplies and munitions. The return of prosperity and the special war taxes produced a current surplus of \$84 million for the year ending March 31, 1917, which slightly more than covered the ordinary capital requirements. The war expenditures had to be met by borrowing. Fifty million dollars were obtained in New York. The remainder was raised in Canada.

During late 1916 and early 1917, the expansion of bank credit got under way in earnest. The banks advanced \$100 million to the Imperial Munitions Board for expenditures in Canada and established a revolving credit of \$20 million for the Imperial Government for the purchase of wheat. They supplied the Canadian Government with \$100 million by the purchase of its treasury bills. Current bank loans to business rose by \$73 million between March, 1916 and March, 1917. These increases in purchasing power were an important factor in bringing about a swift rise in

⁹Wages in certain war industries and of certain unskilled groups rose more rapidly than the cost of living, but the wage rates received by a large section of labour, particularly the skilled trades and the white-collar class, fell behind the rise in the cost of living. The Dominion Department of Labour index of the general movement of wage rates (excluding professional workers and the white-collar class) rose 25 per cent between 1913 and 1917, while the Dominion Bureau of Statistics index of the cost of living rose 31 per cent.

prices and a rapid expansion of production, money incomes and profits. In September, 1916, and March, 1917, the Federal Government floated with ease domestic war loans totalling \$250 million.

In 1917 and 1918, Canada's participation in the struggle became more and more extensive and the costs of financing it increasingly burdensome. In each of these years the Federal Government required between \$500 and \$600 million. The credits granted to Great Britain for her purchases in Canada reached large proportions.

During 1917, the banks made further advances to the Imperial Government amounting to \$150 million for the purchases of munitions and wheat. They continued to finance the Dominion for short periods by taking large amounts of its treasury bills in anticipation of the war loans. Current loans to business rose \$38 million in 1917 and \$217 million in 1918. In these two years the quantity of money (paper notes in the hands of the public and bank deposits) available in the country rose by nearly 40 per cent. This expansion of credit was made possible by the increase in the cash reserves of the banks brought about by the action and policies of the Federal Government. In 1917 there was another fiduciary issue of Dominion notes of \$50 million bringing the total to \$90 million since the beginning of the War. In addition, large amounts of Dominion notes were issued to the banks by rediscounting their securities under the Finance Act. Imperial Government treasury bills held by the banks were rediscounted at $3\frac{1}{2}$ per cent, a rate considerably below the market rates of interest. With the machinery provided by the Finance Act, the banks could increase their cash reserves to any extent that their lending opportunities made profitable. At the end of 1918, bank cash was more than double, and deposits nearly double of what they had been at the end of 1913.

The rapid expansion of credit both in Canada and abroad produced a swift rise in prices. Between 1916 and 1918, the Canadian wholesale price level and the cost of living rose 51 per cent and 34 per cent respectively. The rate of earnings of a considerable section of the community, however, rose more slowly. Real wage rates of large groups of labour (principally the skilled trades and the white-collar class) were appreciably below 1913. The decline in the real income of many wage-earners and of investors in pre-War bonds and mortgages resulted in a rapid increase in business profits, which, together with the rise in the national money income, the war-time increase in thrift and the

reduction in private investment made available large funds for the Federal Government. During the fiscal years ending March 31, 1918 and 1919, the Dominion obtained (net) by means of domestic loans \$516 million and \$589 million respectively. The relative, and in some cases absolute, decline in the standard of living suffered by certain groups, the increase in savings, and the postponement of needed capital facilities helped to make these war loans possible and represented the sacrifices necessary for the conduct of the War.¹⁰ The effects of the inflation spread these sacrifices unequally.

During the War, the taxation imposed by the Dominion was rapidly extended in scope but the increased returns did little more than meet the ordinary current and capital requirements and the interest on the sharply mounting debt. In 1917 the business profits tax was raised and a Dominion income tax was levied for the first time. In 1918 the exemptions for the business profits tax were lowered and the income tax increased. Excise taxes were imposed on a number of luxuries, including motor cars. During the fiscal year ending March 31, 1919, the special war taxes yielded \$56 million or 18 per cent of the total current revenues.

Although the War ended in November, 1918, the heavy cost of demobilization and soldiers' civil re-establishment kept Dominion expenditure at war-time levels for another year and a half. The expansion of bank credit and the precipitous rise in prices continued into the first half of 1920. In the autumn of 1919, the final domestic war loan which produced about \$600 million, was floated.

The transition from war to peace was accomplished with remarkable ease. Half a million soldiers were re-absorbed into civil pursuits without much unemployment or industrial disturbance. The large gap left by the abrupt stoppage of munitions orders was quickly filled by new demands. Exports to war-torn Europe continued at a high level on the basis of large American loans. The Dominion advanced \$46 million to foreign countries which was used to buy goods in Canada. There was a strong demand not only for foodstuffs but also for manufactures. The exports of the latter rose to \$391 million in the year ending March 31, 1920. Much of the slack due to the cessation of war orders, particularly as it affected the steel industry, was taken up by the shipbuilding

¹⁰The huge amount of material goods and services required for the prosecution of the War was largely provided by the increase in production. The problem, however, was to divert this production from private consumption and investment into the hands of the Government. The policies followed to bring about this diversion caused some groups to give up relatively more than others.

program for the Dominion and foreign governments.

The stimulus from abroad was reinforced by internal developments. The cessation of the War was followed both by an upsurge of consumer-buying and a sharp increase in construction activity. The provincial and municipal governments quickly began to provide the community facilities and the developmental projects which the War had postponed. The Dominion increased its outlay on public works, made large expenditures in consolidating and equipping its railway system and granted loans to provinces for the construction of houses. Private industry expanded its equipment and built up inventories. There was an inrush of American branch plants. These activities, capped by the Dominion's heavy outlay on demobilization and the civil re-establishment of soldiers, maintained the post-War boom until the summer of 1920, when the world-wide deflation forced its collapse.

*War-time Regulations of Business and Industry—
its effects on social philosophy and the post-
War expansion of government responsibilities*

The beginning of the post-War depression marks the end of an important phase of Canadian development. The War had wrought many profound changes in public finance, in the economic structure of the country, in social conditions, and in the public conception of the role which governments ought to play in society. Before summarizing the transformation made by the War in the financial position of the Dominion, it is important to note the extent of government intervention in economic life which the War-effort involved because it was a significant factor in changing the popular view of the appropriate sphere of governments.

The first objective of the Federal Government was to win the War and it tried to order all effort to that end. Where it seemed imperative for its purposes the Government undertook to direct the employment of the economic resources of the country. It encouraged in every possible way the production of munitions, and exhorted Canadian farmers to increase their production of food as greatly as possible. But many of its efforts went beyond encouragement to active intervention and control. The scarcity of certain vital supplies led it to undertake the rationing of them in a way calculated to assist its efforts. When the inflation connected with the financing of the War drove the cost of living steeply upward, the Government sought to limit its

unequal effects by imposing further economic controls on business. By the conclusion of the conflict, the Federal Government was in possession of far-reaching powers over economic life. The fact of an unprecedented emergency ensured the constitutional validity of the measures of economic regulation which were adopted.¹¹

From the very early days of the War, the Government exercised a number of unusual powers such as the censorship of the press and cable despatches. However, it was not until the later days, when the inflation had manifested itself in the cost of living, and serious shortages of essential materials began to be felt, that extensive economic regulation was undertaken. In November, 1916, an Order in Council forbade hoarding and accumulation of the necessaries of life. Persons with excessive stocks of these articles were required to sell them at reasonable and just prices and the Government was given wide power to investigate and punish violations. In 1918 housing rentals became subject to the same regulations as other necessaries and municipal councils were authorized to establish Fair Price Committees to investigate the prices of necessaries and publish their determinations of a fair price.

In 1917 the Government assumed control of the marketing of Canada's principal product. The Allied Governments had become virtually the sole foreign buyers of Canadian wheat and they needed it at any price. Thus with the prospect of a short crop in 1917, it became probable that the normal market mechanism would result in famine prices. The Canadian Government intervened on behalf of the Allies by establishing a Board of Grain Supervisors with power to investigate all sources of supply and to ration the available grain between domestic millers and the Wheat Export Company, which was the North American purchasing agency for the Allies. This Board fixed export and domestic prices and controlled the marketing of the 1917 and 1918 crops. It was succeeded in 1919 by the Canadian Wheat Board which acted as an exclusive marketing agency for the crop of that year, superseding the normal marketing facilities of the Canadian grain trade.

As the prices of the necessaries of life, particularly food, continued to rush upward, the Food Control Office was established in 1917 with powers to inquire into available supplies and the reasons for high prices, to determine Canada's food requirements, and to facilitate the export of surpluses. It

¹¹ Cf. *Fort Frances Pulp & Paper Co. v. Manitoba Free Press*, [1923] A.C. 696, with *In re Board of Commerce Act*, [1922] 1 A.C. 191 and see pp. 67-8, *infra*.

was also given power to fix prices and to regulate consumption. In 1918 its powers were transferred to the Canada Food Board which was authorized to direct the production, conservation and distribution of foodstuffs.

The Board licensed, and imposed a variety of restrictions on, processors and dealers in foodstuffs. Although, with a few exceptions, it did not attempt to ration consumption, it did ration the bulk distribution of various commodities among processors and dealers. Importers and exporters were licensed and the use of grain in distilling liquor was prohibited. Public eating houses were subjected to close supervision.

Although the Food Board did not attempt to fix retail prices, it established, in co-operation with the Board of Grain Supervisors, a fixed spread between the price of wheat and the price of flour. It also fixed the price to be paid to the British Columbia fishermen for salmon. Separate Orders in Council fixed the price of newsprint for Canadian consumers and limited the profits of the packing industry by providing that profits in excess of a fixed rate should become the property of the Government.

The coming of the Armistice did not reverse the upward trend in the cost of living. In the face of public clamour over high prices, many of the powers which the Government had exercised under the authority given by the War Measures Act were conferred by Parliament on the newly created Board of Commerce. The Combines and Fair Prices Act of 1919 continued the former prohibitions against hoarding and undue enhancement of the price of necessities. It gave the Board of Commerce power to make exhaustive investigations and to determine a fair profit and a fair price. For a period in 1919-20 the Board exercised its powers vigorously, fixing prices of a wide variety of commodities. But this intense activity was short-lived and price-fixing came to an end before the legislation under which it was exercised was held to be unconstitutional by the Privy Council in 1922.¹²

This review of the economic regulation undertaken by the Federal Government is not exhaustive. It is designed rather to illustrate the extent to which the Government took power to direct the economy during the War. The dislocation of normal activity and the concentration of economic resources for War purposes drove it from one intervention to another. For example, the entry of the United States into the War in 1917 threatened an acute shortage in Canadian coal supplies. Accordingly,

a Fuel Controller was appointed and comprehensive regulation of the coal trade was set up. The Fuel Controller allotted available supplies among the separate provinces. Provincial coal administrators distributed it among communities while local coal committees tried to allot it equitably within each community. Attempts were made to control prices by fixing margins of profit.

The failure of wages in many occupations to keep pace with rising prices was reflected in a great increase in industrial strikes in 1917 and 1918. These seriously hampered production at a time when every effort was being strained to increase production. Consequently strikes and lockouts were forbidden in 1918. Finally, the establishment of the War Trade Board in February, 1918, revealed the full logic of the War economy. The Board's sweeping powers authorized it to carry out "such supervision as may be necessary of all industrial and commercial enterprises. . ."¹³ It was given power to direct the use of the economic resources of the country and to discriminate between "essential" and "less essential" industries by establishing priorities in the right of access to scarce materials among the different industries. Although many of the powers with which the Government armed itself were exercised sparingly and some were not used at all, nevertheless, as the War went on, the economy was steadily being geared to a single purpose.

This dominating purpose disappeared at the close of the War, and with a few temporary exceptions, the unusual economic controls went with it. During the post-War reconstruction period, however, the Federal Government was obliged to undertake new responsibilities. After the long concentration on the War, the return to normal economic activity was in itself a dislocation and it was complicated by the necessity of re-absorbing the citizen army into civilian life. The Government organized a system of pensions for the disabled and for the dependents of those who lost their lives in the struggle. It provided a variety of services to assist in the re-establishment of soldiers in civil life. Through the Soldier Settlement Board it sought to encourage, on a large scale, the settling of returned soldiers on the land. It organized a Dominion Employment Service to co-ordinate the efforts of the provincial employment exchanges. The purpose and the technique of the modern social services became familiar.

As in other countries, the great range of government action during the War had important

¹² *In re Board of Commerce Act*, [1922] 1 A.C. 191.

¹³ P.C. 337, February 9, 1918.

social effects. People saw how governments could mould their lives and civil servants learned how to do it. Statistical and other information necessary for effective intervention in economic affairs was accumulated. The belief grew that governments could and should use their powers to improve social conditions. The War-time experience with the regulation and direction of enterprise was an important factor in bringing on the wide extension of government control which economic and social chaos seemed to make desirable.

War-time Increase in Federal Debt—war and railway nationalization add \$3 billion to liabilities; revenue system greatly expanded to support burden

With the coming of peace, the War-time economic controls were liquidated. For a considerable period, the Dominion refrained from extensive government action for peace-time purposes. It was inhibited by the burden of debt imposed upon it by the War, demobilization and the railway débâcle. The War and demobilization had cost \$1,680 million. In addition, between March 31, 1914, and March 31, 1922, the Federal Government had spent on capital account, excluding the assumption of the guaranteed railway liabilities, about \$1,100 million.¹⁴ During this period the Dominion was required to raise, over and above its ordinary current expenditures, between \$2,700 million and \$2,800 million. Taxation (i.e., the total of surpluses on current account) provided only \$440 million of this amount.

Canada, like the other belligerent countries, met the major portion of its War costs out of borrowings and credit expansion. The imposition of a weight of taxation sufficient to pay for the whole cost of the War was too revolutionary a step to take. The Federal Government had hitherto relied almost exclusively on customs revenues and a few excise taxes. It had no system of general taxation; no machinery for directly taxing the net incomes, profits and wealth of individuals. The sudden introduction of such taxing measures on the scale required was too drastic to be either politically or economically practical. Since Canada was unable to borrow abroad to any great extent, the country as a whole paid for the War while it was being fought. The food, equipment and munitions used by the armies had to be obtained, either directly or indirectly, from current production in Canada

and the producers had to be paid. There was no way of obtaining these materials from posterity. It was, therefore, imperative to increase production and it is doubtful whether that increase would have taken place under the load of taxation necessary to yield the sums required. Individuals and industry are more ready to raise output and produce a surplus (i.e., amounts in excess of current consumption) to be lent to governments at favourable and tax-free rates, than to produce surpluses which governments simply take away by taxation.

Aside from \$135 million (the amount of new issues, less redemptions, floated abroad between the outbreak of War and March 31, 1922) the whole of the loan requirements, amounting to over \$2,100 million, were raised in Canada. The extent to which this money came out of business profits and the incomes of the well-to-do (the increases in which arose, in considerable part, out of the effects of the inflation) is indicated by the fact that from 80 per cent to 85 per cent of the War-loan bonds were purchased by business organizations, financial institutions, and individuals with substantial incomes.

The War costs and other capitalized expenditures resulted in an increase of \$2,300 million in the debt of the Dominion. The assumption of the guaranteed and other liabilities of two transcontinental railways added a further \$700 million. At the outbreak of hostilities, the Canadian Northern and the Grand Trunk systems had not been completed. It had, however, become increasingly clear that these gigantic projects which the Federal and Provincial Governments had assisted liberally with subsidies and guarantees were doomed to failure. The duplication of expensive lines through unproductive territory could only be justified on the basis of a continuation of the 1900-13 boom far into the future. The 1913-14 depression was a significant warning that this would not happen. The War, which almost completely shut off immigration and capital imports, brought an end to rapid frontier expansion. The situation was further aggravated by the rise in prices and the inability to borrow in the London money market. The increased cost of construction added still more to the heavy fixed charges and the rapid rise in operating expenses enhanced the distressing deficits. Unable to borrow abroad, even on their government guaranteed securities, the companies were entirely dependent upon temporary loans and advances from the Dominion.

By 1916 the situation had become critical. The Dominion was faced with three alternatives. The first was to allow the companies to go into bank-

¹⁴\$640 million were spent on railways and canals, \$116 million on public works, \$80 million on soldiers' settlement, \$155 million net on advances to the United Kingdom and foreign governments, and about \$110 million on miscellaneous works and advances.

ruptcy and thus, after a long legal battle and a possible deterioration of service and equipment, secure a reduction in their fixed charges. The second was to continue making advances to keep them going, and the third, to take over the roads and assume their liabilities. The Railway Inquiry Commission of 1916 recommended the last course. The bankruptcy of the companies and default on their securities, it was feared, would be ruinous to the credit of the country. Furthermore, there was danger that the freezing of the temporary loans made by financial institutions to the Canadian Northern would cause a financial panic in Canada. Thus, between 1917 and 1922, the Canadian Northern and the Grand Trunk Pacific were taken over together with the Grand Trunk and consolidated with the Canadian Government railways into one system, the Canadian National. All the debenture liabilities of the companies, including as well those on which there had been no guarantee and those guaranteed by the provinces, as well as those which the Dominion had guaranteed, were assumed by the Dominion.¹⁵ Practically the whole of the capital expenditures on the newer roads had been financed by the sale of these fixed-interest securities. There was virtually no equity investment. The entire cost of these misguided private ventures was, therefore, loaded on the shoulders of the taxpayer with very little loss to the private investor. Thus a heavy overhead on the economy undertaken at private risk was converted into fixed charges of government.

The total direct and indirect debt of the Federal Government (accounted for almost entirely by the War and the railways) rose from half a billion in 1913 to three-and-a-half billion in 1921. During the same period expenditures on current account rose from \$118 million to \$354 million. Of this increase, 56 per cent was due to debt charges, 22 per cent to War pensions, and the remainder largely to the higher price and wage levels at which the ordinary services of government had to be provided. Prior to 1914 the entire current expenditures of the Dominion were devoted to supplying services to the community. About 50 per cent (including all the debt charges) were for developmental purposes, about 40 per cent for general government and defence and 10 per cent for subsidies to provinces. In 1921 almost half of the total outlay consisted of transfer expenditures which yielded no immediate services. Nearly \$100

¹⁵ The securities guaranteed by the provinces and those on which there was no guarantee were not technically or legally assumed by the Dominion, but were assumed in fact since the Dominion paid the interest and met the maturities as they became due.

million of interest payments was on debts for which there were no productive assets, and \$54 million was expended on soldiers' pensions and aftercare. These two items constituted a mere transfer of income from the taxpayers to the holders of bonds (largely tax-free War loan bonds) and to pensioners. They neither added to, nor took away anything from, the sum total of goods and services enjoyed by the country as a whole.

The new transfer expenditure was the principal factor which forced the War-time and immediate post-War widening of the Dominion's revenue base. In 1913, 78 per cent of the total receipts came from customs duties, and the remainder largely from the excise on liquors and tobacco. In 1921 the proportion from customs had fallen to less than a third; a sales tax, income taxes on corporations and persons, a business profits tax, and a miscellaneous series of taxes on financial institutions, transportation tickets, cheques, etc., had been added to the revenue system. Virtually the whole of the two-and-a-half fold increase in revenue since 1913 was obtained from the new taxes.

The \$150 million of transfer expenditures were very largely a legacy of the War costs to which wage-earners and others with low incomes had been called upon to contribute more than their share. The Dominion tax system now forced wage-earners and other low income groups to carry the major part of the post-War burden. The progressive taxes (taxes on the incomes of persons and on business profits) yielded but \$63 million. The remainder of the new revenue was mainly derived from sales taxes and a proportionate tax on the net incomes of corporations. The imposts on consumption not only fell heavily on the poor but were a deterrent to industry. The taxation measures adopted by the Dominion to meet the obligations inherited from the War were a revolutionary change from the simple system of pre-War days. They were, however, far from being the most equitable and efficient that could be devised.

Provincial-Municipal Finance—the War-time restraint on expenditures; sharp increases in debt and expenditures on public welfare during 1918-21

The steep increase in provincial and municipal debts and expenditures, which had been characteristic of the 1896-1913 period, had already been checked by the depression which set in shortly before the outbreak of hostilities. During the War the difficulty of borrowing abroad, the diversion of

domestic investment funds into Federal channels and the search of the Dominion for additional revenues, effectively restrained the expansion of provincial and municipal activities. For several years after 1913, the latter governments marked time or fell back. As soon as hostilities ceased, however, they rapidly embarked upon new expenditures, and by 1921 the upsurge which marked the early years of the century had been resumed.

TABLE 22.—GOVERNMENT DEBTS, DIRECT AND INDIRECT
—1913 AND 1921

	1913		1921	
	Total	Per Capita	Total	Per Capita
	\$000	\$	\$000	\$
Dominion of Canada and Canadian National Railways	520.8	68	3,520.0	400
Provinces.....	285.0	37	622.3	72
Municipalities.....	504.6	65	803.7	91
Sub-Total.....	1,310.4		4,947.0	
Less Inter-governmental Debts—				
Dominion-Provincial.....	11.5		49.7	
Provincial-Municipal.....	0.9		24.5	
Total.....	1,298.0	170	4,862.8	556

The most striking feature of the public finance of the provinces and municipalities during this period was the rapid increase in debts immediately after the close of the War.¹⁶ This rush of capital expenditures was in response to far-reaching technical, economic and social changes. Already in 1914 the effects on provincial-municipal finances of the motor car, the development of electricity and the long distance transmission of electric power were beginning to be felt. The heavy capital outlays demanded by these changes had been postponed by the War, but were undertaken with great vigour once hostilities ended. The increasing use of the automobile necessitated an almost complete reconstruction of urban streets and traffic facilities. The provinces began to build trunk highways and to assist in the improvement of roads generally to motor car standards. More than one-fourth of the \$650 million increase in provincial-municipal debt during 1913-21 was incurred for capital expenditures on highways, streets and bridges.

Public utilities (excluding railways) accounted for some 40 per cent of the rise in total provincial-municipal liabilities. Ontario spent more than \$100

million on Hydro. Provincial power commissions were established in Manitoba, New Brunswick and Nova Scotia. The three Prairie Provinces doubled their investments in telephones. Many municipalities expanded and improved their water systems. The cities of Saskatchewan, Manitoba and Ontario expended considerable sums on electric power facilities and in some cases on street railways. While the extension of public utilities added substantially to gross debts, these did not increase the burdens on the taxpayer since they were virtually all self-supporting.

The greatest increase in deadweight debt arose out of the large outlays on public buildings and miscellaneous works. The industrial expansion and urbanization stimulated by the War, together with the new responsibilities for social welfare, added considerably to the size and variety of buildings and institutions required for public purposes. These demands fell most directly on the municipalities. In the rapid extension of such facilities, together with the large expenditures on streets, sewers and waterworks, many urban centres practically rebuilt their entire capital equipment during the few years after the War. The expenditures were largely financed by 12 to 15-year debentures, a period much shorter than the life of the assets if they were fully maintained. Thus, while debts rose rapidly during 1918-21, they were scheduled to decline rapidly during the thirties when the bonds would mature.

The provinces, in addition to the demands for highways, buildings and public utilities, had to cope with the problems of the post-War depression and drought. British Columbia, Manitoba and all of the Eastern Provinces undertook housing programs financed by loans from the Dominion. Prairie agriculture, hampered by short yields, high interest rates and sharp price declines (after 1920) called for special assistance. The provincial governments attempted to relieve the situation by the provision of agricultural credit, seed grain loans, loans to farmers' co-operatives and by advances to an irrigation project in Alberta. Thirty-four million dollars were advanced for these purposes, and most of this sum soon proved to be uncollectable.

The rapid increase in the new commitments by the Western Provinces was greatly facilitated by the Dominion's assumption of \$85 million of their railway guarantees. The relief from this threatening load gave scope to the provinces for response to many demands which, however, quickly substituted other heavy deadweight burdens.

¹⁶ Between 1913 and 1921, the total per capita provincial and municipal debts rose by over 60 per cent; practically all of the increase was incurred during the three years following 1918.

TABLE 23.—GOVERNMENT EXPENDITURES, CURRENT ACCOUNT, 1913 AND 1921

(Thousands of Dollars)

	Municipal		Provincial		Dominion		Total ^(a)	
	1913	1921	1913	1921	1913	1921	1913	1921
Net Debt Charges.....	19,713	36,944	2,304	14,384	12,213	162,488	34,794	202,475
Defence.....	—	—	—	—	13,781	17,249	13,781	17,249
Pensions and Aftercare.....	—	—	—	—	94	53,688	94	53,688
Public Welfare.....	8,161	18,786	4,343	12,437	2,617	4,911	15,121	36,134
Education.....	27,700	66,280	9,900	20,850	215	924	37,515	88,057
Agriculture and Public Domain.....	—	—	7,434	9,174	10,985	17,596	18,403	26,722
Transportation.....	14,699	30,962	8,631	8,119	35,467	41,666	56,663	80,747
Subsidies to Provinces.....	—	—	—	—	11,280	12,212	—	—
General Expenditures— Justice, Legislation, General Government and Miscellaneous.....	30,125	51,911	15,069	25,689	31,642	^(b) 53,733	76,836	^(b) 131,333
TOTAL.....	100,398	204,883	47,381	90,653	118,294	354,467	253,207	636,405

^(a) Inter-governmental payments eliminated.
^(b) Includes Post Office deficit of 4,045.

Between 1913 and 1921 the current expenditures of the provinces and municipalities were each approximately doubled. In the interval, however, the price level had risen by about 70 per cent and the population by about 15 per cent. Making allowances for these factors, there were no significant changes in the total real per capita outlays. The War, which had added about 70 per cent to the real per capita expenditures of the Dominion, curbed the activities of the other levels of government. In the last three years of the period, the provincial and municipal response to the demands which had accumulated during the conflict took the form of large expenditures on capital, rather than on current account. Although net debt charges had more than doubled, the full burden of the new liabilities was not felt until later when many of the provincial advances and investments failed to be self-supporting.

While the total per capita real outlay of the provinces and municipalities on ordinary account did not increase, significant shifts occurred in its distribution among the various services. Public welfare expenditures were nearly trebled, reflecting a new attitude concerning the appropriate functions of government resulting from the impact

of the War and the changing economy on social conditions. There were new services such as mothers' allowances and child welfare; there were enhanced expenditures on mental hospitals, a joint Dominion-provincial campaign against venereal disease, and, by 1921, a new and ominous item arising out of the brief but severe post-War depression, direct relief for the unemployed. Current expenditure on education was also higher. Here, as in public health, the Dominion Government had stepped in to inspire and direct new provincial schemes by the use of conditional grants. By 1921 these extended to employment service, the control of venereal disease, technical and agricultural education, and highways. Contributory payments were also being made by the Dominion to meet unemployment relief.

The expansion in these branches made relative, and in some cases absolute, reductions necessary elsewhere. The outlays on general government, justice and legislation declined in the eight years when allowance is made for the rise in wages, prices and population. Public domain, agriculture and transportation had to wait their turn until revenues again became more buoyant, as they did in most provinces early in the twenties.

TABLE 24.—GOVERNMENT REVENUES, CURRENT ACCOUNT, 1913 AND 1921

(Thousands of Dollars)

	Municipal		Provincial		Dominion		Total ^(a)	
	1913	1921	1913	1921	1913	1921	1913	1921
Federal Subsidies.....	—	—	12,851	11,865	—	—	—	—
Taxes—								
Customs Import Duties.....	—	—	—	—	104,691	105,687	104,691	105,687
Excise Duties.....	—	—	—	—	21,452	36,755	21,452	36,755
Manufacturers' Taxes.....	—	—	—	—	—	6,639	—	6,639
Sales Taxes.....	—	—	—	—	—	61,273	—	61,273
Corporation Taxes.....	—	—	3,490	11,162	—	64,008	3,490	75,170
Succession Duties.....	—	—	3,611	9,724	—	—	3,611	9,724
Income Taxes on Persons.....	38	73	119	485	—	39,821	157	40,379
Real Property Taxes.....	90,314	189,656	1,753	9,720	—	—	92,067	199,376
Amusement Taxes.....	—	—	—	3,032	—	—	—	3,032
Other Taxes.....	6,517	17,956	347	1,199	1,335	6,140	8,199	25,295
Sub-Total—Taxes.....	96,869	207,685	9,320	35,322	127,478	320,323	233,667	563,330
Motor Vehicles, Automobile licences, etc....	—	—	470	8,381	—	—	470	8,381
All Other Licences, Permits and Fees, Fines and Penalties.....	5,004	8,010	6,678	8,360	1,516	2,860	13,198	19,230
Public Domain.....	—	—	11,046	14,786	3,420	3,542	14,466	18,328
Liquor Control.....	—	—	2,248	7,856	—	—	2,248	7,856
Sale of Commodities and Services.....	305	1,155	815	747	1,513	2,358	2,633	4,260
Other.....	7,697	13,537	1,507	3,083	1,276	3,425	10,089	18,679
TOTAL.....	109,875	230,387	44,935	90,400	135,203	332,508	276,771	640,064

^(a) Later-governmental receipts eliminated.

The growth in population and the rising prices and wages which added substantially to the total money cost of government did not, however, produce an equivalent increase in the receipts from the existing revenue sources and tax rates. But new and additional revenues were readily found. Owing largely to the rise in land values in the medium-sized industrial cities of Eastern Canada, the municipalities were able to double their aggregate income from real property taxes with relative ease. In the case of the provinces, a number of the factors which were adding to their burdens also extended their sources of revenue. The growing concentration of control in industry and finance and the large profits made by individuals and corporations out of the War-time prosperity, enlarged the pools of wealth which could be tapped by corporation taxes and eventually by succession duties. Total receipts of provincial governments from these taxes rose from \$7 million to \$21 million during the period. As before, however, some provinces had a much greater access to these sources than others; Quebec, Ontario and British Columbia received more than three-quarters of the total. The grow-

ing motor traffic which was forcing the provinces into large expenditures on highways also opened up new sources of revenue. Motor licences, which provided a paltry sum in 1913, were yielding more than \$8 million by 1921. In the Prairie Provinces, where high prices for wheat and other agricultural products inflated land values, the provincial governments levied taxes on real property which in 1921 brought in over \$7 million. Quebec and British Columbia, which by the end of this period had abandoned the War-time experiment of prohibition and made the sale of liquor a government monopoly, were already collecting substantial amounts from liquor control.

The federal subsidies, which remained unchanged throughout this period, had by 1921 fallen in relative importance to only 13 per cent of total provincial revenues. New and increased government responsibilities, and technical and social changes had, by the end of the War, advanced the public finances of the provinces a long distance from the simple dependence upon licences and fees, public domain and federal subsidies.

Basic Effects of the War on the Canadian Economy—large increase in export production, and development toward financial and industrial maturity

Canada's part in the War had cost her great sacrifices in men and money. However, the very necessities and demands of the conflict had revealed, and speedily developed, a wealth of resources and capacities which, notwithstanding the enormous waste of the struggle, brought very substantial and permanent gains to the economy.¹⁷ In 1914 the country was confronted with a painful adjustment from a prosperity dependent upon capital imports and a construction boom to a large expansion in export production. The requirements and circumstances of the War made the transition easy and rapid. The resources and men threatened with prolonged unemployment were quickly drawn into industry. The productive capacity of the country was greatly increased.

The expansion in its main features took place within the pattern laid down by the national economic policies during 1896-1913. The development of an integrated transcontinental economy was continued on the basis of a predominantly exporting region in the West and an industrialized East dependent upon the home market. In the Prairie Provinces the acreage in field crops increased 84 per cent between 1914 and 1920. During these years the population of this area rose 19 per cent compared with 9 per cent for the country as a whole. Canada's main economic contact with the outside world, its principal stimulus to expansion, grew greatly in importance. This progress of Western agriculture, however, was not achieved without the creation of problems. In the later years of the period crop yields were poor and as prices were relatively high the incentives to expand were great. Much of the increase required in equipment, land and buildings was obtained at high prices by means of borrowed money. Considerable land which was later to prove sub-marginal was brought under the plough. The debts were to become difficult to carry and the sub-marginal farms unprofitable when prices fell.

While the Prairie Provinces retained their position as the dominant exporting region, there were important developments in other areas based upon foreign markets. The War gave a considerable impetus to the production of non-ferrous metals. Improved processes were developed for the treatment of ores and their conversion into refined

products. The production of pulp and paper became a major industry. (The output of pulpwood nearly doubled and the value of the exports of pulp and paper increased five-fold.) Hydro-electric power played a significant role in these developments. Capital invested in central electric stations rose 80 per cent. The natural resources of northern Ontario and Quebec and British Columbia gave rise to important new export areas which found their outlets chiefly in the United States. The simple East-West structure of the Canadian economy was becoming complicated by new economic frontiers and new external relations.

The influences of the War enhanced the position of Central Canada as the source of manufactured goods, and commercial and financial services for the exporting regions in the other parts of the country. The decline in exports from Europe and the high cost of shipping enabled Canadian manufacturers to obtain a larger share of the home market. Although the munitions orders came from overseas and were but a temporary factor, they had important long-run effects. The demands imposed and the facilities required to meet them resulted in a considerable increase in technical and mechanical efficiency. The demand for munitions produced also a much needed diversification, particularly in the iron and steel industry which had been highly specialized to supply the demands of railway building and heavy construction. This progress in efficiency and diversification was greatly facilitated (as was the case in the production of munitions) by the availability of skilled labour, tools, machinery and supplies from the United States. The Canadian manufacturing industry emerged from the War with a more dominant place in the domestic market, with an enlarged productive capacity, and with much improved and diversified facilities.

The financing of the War promoted a rapid development of financial institutions. The sale of over \$2,000 million of War loan bonds stimulated the growth of security underwriting and distributing organizations. Experience was gained in the technique of mobilizing the savings of the country and Canadians generally became more familiar with the investment market and accustomed to the purchase of securities. By the end of the War the Canadian economy had acquired an extensive and quite a mature financial equipment.

The growth of manufacturing and finance accentuated the concentration of national secondary and service industries in Central Canada. Between 1911 and 1921, the urban population of Ontario and Quebec rose from 50 per cent to 57 per cent of the

¹⁷ It is not suggested that a greater gain might not have been made had Canada not been engaged in the War.

total population of these provinces. During the same period, the population of the metropolitan areas of Montreal and Toronto grew by 38 per cent compared with 22 per cent for the country as a whole. The integration between the various parts of the transcontinental economy was increased and the dependence of the St. Lawrence-Great Lakes area upon the other regions of the country became more complete.

The War brought significant changes in Canada's external economic relations. Prior to 1914 the relations were mainly with Great Britain, which took slightly more than half the exports and was the principal source of the capital imports. In the post-War period the relative position of Great Britain, as a market for our products and as the source of both capital and merchandise imports, had declined. This change was chiefly due to the growing importance of the United States, whose share in the Canadian import and export trade rose from about 50 per cent to 60 per cent of the total. When the War made it impossible to borrow in London, Canadian industry, provinces and municipalities turned to New York. Between 1913 and 1921 the total United States investment in Canada rose from \$780 million to \$2,300 million while the total British investment fell slightly. Both with respect to Canadian banking and investment connections, New York surpassed London in importance.

The development of Canada's natural resources during the War had greatly increased her capacity for export production. On the other hand, the higher price level made it easier to carry the external debts contracted at pre-War prices and interest rates. While the country's economic position with respect to the outside world was improved, the economy remained highly sensitive to external fluctuations. The ebb and flow of prosperity was more than ever dependent upon the factors which affected foreign trade and capital movement.

3. THE WAR, POLITICAL AND SOCIAL CHANGES

Weakening of Old Political Parties—political revolt of farm and labour groups; reaction against inequalities in War sacrifices and profiteering

The War had a profoundly unsettling effect upon the whole western world which was only less marked in North America than in Europe. The War upset the habitual routine of people, replaced their normal pre-occupations with exciting distractions and altered the customary relationships between different groups within the community. Canada participated vigorously in the struggle and was

exposed to most of its disturbing influences. The opposition of farmer and labour elements to conscription was symptomatic of deeper discontent. This discontent spread through the farmer and labour groups during the later days of the War and, on the cessation of hostilities in Europe, it broke into open political revolt in Ontario and the Prairie Provinces, resulting in the temporary disintegration of the federal political parties in these provinces.

The federal political parties had been based upon the common acceptance, with varying interpretations and emphasis, of certain general policies. The alliance of powerful groups of agriculture and labour in the progressive movement was based on the view that the old line parties had become organizations to further class interests prejudicial to the general public interest. It involved reliance upon class political organizations as a means of redressing the balance in their favour. The denial that the national policies of the two old parties furthered common national interests was a new political doctrine. The two federal parties had tried to unite elements from both races and all classes around particular interpretations of the national interest. The new movement assumed the contradictory and opposed character of group interests and saw federal politics as an arena where these antagonistic forces struggled for mastery.

There were a number of reasons why this explanation of the nature of the political process made such a wide appeal at the close of the War. In part, it followed from the diversification of the economy which had made such rapid progress since the beginning of the century. This development had increased the number of economic interests and had sharpened contrasts in the relative position of different groups. Differences in relative position were extended, and contrasts were emphasized, by the War. Canada's participation in it brought rewards as well as sacrifices, and both were unequally distributed among the population. Inflation held down the real income of large sections of the labouring and white-collar groups. Although agriculture had prospered where crops were good, there were large areas in the West where crops were poor, or had failed, in the later years of the War period.

There was no general or steep reduction in the standard of living during the War and the position of some labour and agricultural groups improved. However, prosperity and good fortune are always, to a great extent, relative. Psychological factors played a large part in the revolt. There was general alarm and resentment, as well as actual suffering, over the steep and continuous rise in prices. There

was widespread evidence of large profits having been reaped from War prosperity. Popular belief magnified both the size of these profits and the number of people who had shared in them. The profiteer was seized upon as the cause rather than the effect of rising prices, and fierce indignation was levelled at those who conspired to profit from human suffering and misery. The inequality of rewards and sacrifices was real and striking. Popular indignation at these inequities and misunderstanding of the causes behind them made the inequalities seem ever greater and more sinister than they really were.

The Growth of Organized Labour

Labour organization made great strides during the War. Trade union membership increased from 166,000 in 1914 to 374,000 in 1919. Labour was the most directly affected by the rise in the cost of living. The Trades and Labour Congress, after protesting against conscription, finally acquiesced in its imposition. But during 1918 the impatience of the Western wing of the labour movement with the conciliatory tactics of the Eastern section of the movement became very marked. The Western labour leaders, in particular, were indignant over the banning of radical literature by the Dominion Government, and there was considerable resentment over Canada's participation in the "capitalist intervention" in Russia. Having failed to win the Trades and Labour Congress from craft organization to industrial unions at the convention of 1918, the more radical of the Western leaders launched the One Big Union early in 1919 as an industrial union for direct action in the industrial field.

Although the One Big Union had contemplated a general strike, to begin June 1st, it was not officially connected as an organization with the sympathetic general strike which broke out in Winnipeg in May. This struggle raised passions everywhere and stirred the sympathies of labour organizations in other parts of the country. It was followed by a number of strikes elsewhere and seemed to threaten a general crisis in Canadian industry. Then the Federal Government intervened, arresting a number of the leaders. It sought to crush this kind of protest through amendments to the Immigration Act and the Criminal Code. Its action enabled the strike leaders to say that they had been defeated by the Government, and lent impressive weight to the argument that independent political action was necessary to protect the interests of labour. The incident gave impetus to the farmer-labour movement.

The Rise in the Political Power of Organized Agriculture—the election of farmers' governments in Ontario and Alberta and the rise of the Progressive Party.

Farmers' organizations also grew rapidly during the War. The United Farmers of Ontario, first organized in 1914, had secured a membership of 48,000 by 1919. Farmers' organizations on the Prairies had enrolled 75,000 members by that year. Their co-operative commercial enterprises had met with success, and the Canadian Council of Agriculture opened permanent offices in Winnipeg in 1916 from which it began to press vigorously the point of view of the farmers in national affairs. It constructed the so-called "Farmers' Platform" in 1916 and, in November, 1918, an amended form of it was published under the significant title of "The New National Policy". The political revolt was a direct challenge to the older national policies.

The manner in which the Federal Government dealt with the deputation of farmers who protested against the cancellation of exemptions from military service helped to precipitate the United Farmers of Ontario into politics. In June, 1918, a convention was held in Toronto for the purpose of ventilating grievances. Speakers demanded independent political action, and a proposal for an official journal for the movement later resulted in the purchase of the *Weekly Sun*. In October, 1918, a farmers' candidate won a provincial by-election in Manitoulin Island. A spontaneous movement for political action began among the local farmers' clubs. The leaders of the United Farmers of Ontario gave the movement direction and in the autumn of 1919, a farmers' government gained power in Ontario.

Farmers' candidates began to score successes in federal by-elections and, in January, 1920, the National Progressive Party was formed for concerted action in the federal field. Fourteen farmer candidates were elected in the Manitoba elections of that year. In 1921, the United Farmers of Alberta won an overwhelming victory in the provincial elections. In December of that year, the Union Government was defeated disastrously and sixty-five Progressives were returned to the House of Commons.

The Progressive movement, led by the farmers' organizations and strengthened by support from labour, was in the scale it assumed an entirely new phenomenon in Canadian politics although in pre-War years there had been periodic manifestations of desire for independent action. It was remarkably successful in the three years immediately following the War. Previously, movements

of protest from agricultural groups had generally tried to secure expression by supporting and exerting influence upon the Liberal Party. At this time, however, the Liberal Party was completely disorganized in the Federal field and considerably weakened in several provinces by the support given by some provincial leaders to the Union Government. But in a great measure, the prevailing discontent could not have found expression through the Liberal Party because it was directed against the political system of which the Liberal Party was an intimate part. It was a direct reflection of the corrosive social effects of the War.

Summary, 1914-21

The permanent effects of the War upon Canada have not yet been fully realized but some of them, at any rate, have become obvious. It stimulated the economy in various ways. Economic and financial inter-relationships with the United States were multiplied. The necessity of financing the War effort at home brought a quick development of financial machinery, giving the system a maturity it had hitherto lacked. The insatiable demand for supplies advanced the economy rapidly along the main lines projected by the wheat boom. With the rise of new exporting regions and industries and the expansion of wheat growing on the Prairies, the dependence on export markets was greatly deepened. Domestic industry committed itself still further to supplying the needs of the exporting groups. At the same time, the long-range effect of the War was to hamper international trade and to make the grip on foreign markets more precarious. The Canadian economy became still more vulnerable to external influences.

While the struggle lasted, the Federal Government monopolized public attention. The national effort led to a concentration on national issues and finally to bitter division on the national interest. The cleavages on this question followed cultural, class and occupational lines rather than the familiar party division or the alignment of some provinces against the Dominion. The immense authority, born of a common aim, which the Dominion Government exercised during the struggle disintegrated with the return of peace. It became very difficult to combine the group interests, which more and more found expression in Federal politics, for the support of a vigorous policy by the Dominion. Thus, in the event, the partial eclipse of the provinces was short-lived. In the twenties, the provinces were to take a more important place than ever before while the Dominion followed a mainly negative policy.

At the beginning of the period, most of the varied and exciting opportunities which came with western expansion suddenly vanished with the collapse of the boom. Economic diversification continued and people were obliged to apply themselves to highly specialized occupations. As they became less adaptable and less able to make sudden shifts in occupation, the economy lost much of the flexibility and capacity for automatic adjustment to changed conditions which had marked it in the days of the open frontier. Many of the material conditions which had already led the advanced industrial countries of Europe to make public provision for social security were emerging in Canada. The War accelerated this significant change in the economy and contributed to the decline of laissez-faire as a social philosophy. It exacted innumerable individual sacrifices for the community and thus suggested reciprocal obligations of the community toward individuals. The common folk who bore the brunt of the struggle were encouraged to expect that victory would usher in a new era. The new era did not come, but instead the inequality of individual rewards and sacrifices which marked the prosecution of the War sharpened social distinctions. This combination of circumstances stimulated a growing concern for the social welfare of those who must fight the country's battles. Recalling the War-time activity of governments, many were led to hope that governments could organize for social welfare as they had organized for War. The War hastened considerably the acceptance of the philosophy of the social service state in Canada.

The whole burden of the War expenditures fell on the Dominion at a time when it also had to pay the full consequences of the rash railway policies launched during the wheat boom. In seven years, the public debt of the Dominion increased seven-fold. The Dominion was reluctant to undertake new responsibilities, and this paralyzing debt became the financial counterpart of the political weakness which fell upon the Dominion. On the other hand, the War had been a damper on expenditures by provincial governments. After its conclusion, the provinces began without hesitation to make large expenditures to meet accumulated demands. They at once increased their expenditures on social welfare and, although they secured some federal financial assistance through conditional grants, the events of the first two or three years after the War indicated that it would be the provinces, and not the Dominion, which would meet the growing demand for social services.

CHAPTER V

THE POST WAR PROSPERITY 1921-30

Impact of Economic and Social Changes on Federal Relations—decline in unifying influences of national policies and growing diversity of regional interests

In the twenties, the world made a substantial, though temporary and superficial, recovery from the disruption caused by the War. In Canada, the era of reconstruction led to new and impressive expansion. The economic integration based on wheat reached a new peak of productivity which tended to obscure, for the time being, the more significant features of the expansion. The age of steel and steam within which Canadian economic development had hitherto taken place had to make way for the age of alloys, hydro-electric power and the internal combustion engine. The new techniques, the development of which had been forced by the War, opened up vast new Canadian resources for development and heavy investments were made for their effective exploitation. The impact of these developments brought rapid changes in the pattern of the Canadian economy. The national integration (achieved through wheat), which tied the country together by East-West bonds of trade and opportunity was weakened as Central Canada and British Columbia felt the direct and competing tug of export demand on their regional resources. New economic frontiers, the exploitation of which was of primary interest to Ontario and Quebec, developed on the Pre-Cambrian Shield,—where water power, base metals and pulp and paper came into their own,—and began to usurp the place of the old national frontier in the West. In the successful development of these new frontiers, the importance of a national economic integration for some regions declined and the material basis which had bolstered political unity in the past was measurably weakened.

In the past, the Dominion had been able to prosecute with vigour certain national policies which promoted national integration because of the common interest of all regions in the result. As these national policies lost some of their unifying power, the common agreement necessary for resolute political action by the Dominion became more difficult to secure. Still more important, with

the opening of the West finally and fully accomplished, it seemed that many of the national economic policies had been carried to completion. No obvious and pressing challenge to action presented itself in the federal sphere in this period. To many it seemed that the time had come when the Federal Government might rest from its arduous labours and muse over how it had justified the faith of the Fathers. For other reasons, the Dominion was much disposed to rest. The War had strained the federal political system and set various groups at odds over the national policies. The national debt had been increased several-fold. In seeking to reduce its old obligations and to avoid new ones, the Dominion yielded the initiative to the provinces.

By contrast, the provinces, which had suffered enforced restrictions on their activities during the War, were not unwilling to undertake leadership on their own account. The natural resources which the new techniques opened up for exploitation were under their control and this gave the provincial governments an enhanced importance in the eyes of private enterprise.

Several factors combined to give a new political importance to the provinces. Highway construction and developmental projects on the provincial frontiers began to take the place which railway construction and national projects of development had occupied in the past. In the jobs and contracts which were thus at the disposal of the provincial governments, there were substantial increments of political power. Moreover, in the twenties, the social and political implications of the change from a simple rural and village economy to a highly specialized, predominantly industrial economy could no longer be ignored. The mischances which befall individuals in such a society could no longer be cushioned by the family and voluntary charity. The constitution threw the responsibility for public welfare on the provinces (and municipalities) and within the limits of their resources they tried to meet it. These activities brought the provincial governments into a closer relationship with the people. In their intimate contact with the movements and tendencies of the time, the provincial governments added greatly to their economic and

social importance and thus to their political power and prestige. Those which could carry their obligations manifested a new independence of the Federal Government and those which could not became more importunate as they focused on the Federal Government regional protest against the operation of the national policies. In the endeavour to meet their growing obligations or to take full advantage of rising economic opportunities, provincial demands of various kinds were made on the Dominion, and the Federal Government, unable to deflect these demands by a vigorous policy of its own, made important concessions to the provinces. The rise of regionalism gave an altered direction to Dominion-provincial relations.

Regionalism reflected differences in interests and opportunities which had become quite pronounced in different parts of Canada. The various regions had always differed in resources and geographical advantages. These promoted economic specialization and made for disparities in the fortunes of separate areas. The national policies, which had both hastened and deepened specialization, played continuously on the regional disparities, sometimes counteracting, but often exaggerating, them. With so large a dependence on exports, fluctuations and shifts in international trade capriciously moulded regional fortunes. A long lag in recovery from the post-War slump revealed serious weakness in the Maritimes which was met, in some measure, by an increase in federal subsidies. The decline in export values in the early twenties, and again at the end of the period, made clear the overwhelming dependence of the whole structure of Prairie government finance on wheat. On the other hand, Central Canada forged ahead rapidly without interruption throughout the period. At the same time, the increasing need and demand for certain minimum public services bore little relation to the capacity of the governments in a region to supply them. The great disparities in the strength of the regional economies were temporarily obscured by the surge of prosperity which carried provincial and municipal expenditures and obligations to new heights in the later twenties. At the same time, the very factors which brought prosperity made the economy more vulnerable than ever before to economic fluctuations. With the coming of depression at the end of the period, these new conditions were fully exposed to view and some of their implications became inescapable. Federal action became necessary to maintain a tolerable equilibrium between the regions in the federation.

1. PROSPERITY AND THE CHANGING STRUCTURE OF THE ECONOMY

World Influences—short post-War depression; reconstruction and revival of international trade and investment bring renewed expansion to Canada.

At the end of the Great War Canada found herself in an economic world which was utterly disrupted. International trade was hampered by a maze of national restrictions and controls. The international exchanges were in a state of desperate confusion and instability. Important industries, particularly shipping, coal mining, iron and steel, and heavy engineering had expanded beyond peacetime requirements. Large masses of Europe's population suffered from grave shortages of food-stuffs and raw materials. The staggering load of internal and external debts, and the heavy expenditures on social services and rehabilitation, forced a continuance of unbalanced budgets which, in many cases, resulted in uncontrolled inflation. The intricate mechanism of money and exchange which was the basis of the world's economic life seemed broken almost beyond repair. The passions of the conflict, deep underlying grievances, and revolutionary tendencies enhanced the difficulties of reconstruction.

In 1920 these far-reaching dislocations brought about a collapse of the short post-War boom. The liquidation of the world-wide inflation of credit had an immediate effect upon Canada through the steep decline in export prices and demand.

TABLE 25.—INDICES OF PRICES AND EXPORTS⁽¹⁾

	All Wholesale Prices	Export Prices	Farm Products	Wheat Prices	Manufactured Goods Prices	Cost of Living	Value of Exports	Volume of Exports
1920.....	100	100	100	100	100	100	100	100
1921.....	71	74	64	66	74	88	64	87
1922.....	62	60	55	49	64	81	71	118
1923.....	69	59	51	43	66	81	80	136

⁽¹⁾ Dominion Bureau of Statistics price indices.

The movement of prices had drastic effects upon the Canadian economy, not so much because of the extent of the fall (although it was one of the most severe ever experienced following an almost equally abrupt rise) but because of the great disparities which developed. Selling prices (wholesale prices) fell more rapidly than costs (cost of living, wages,

freight rates, interest rates, etc.). Agricultural prices, particularly that of wheat, fell far out of line with the prices of manufactured goods and the cost of living. During the rapid expansion of the War years, Prairie farmers had incurred heavy debts, purchased much machinery, equipment and land at the high War prices.¹ When the value of wheat fell by more than 50 per cent, it became virtually impossible to carry these overhead costs and commitments. The situation was further aggravated by the United States tariff increases of 1921 and 1922 which sharply restricted the substantial exports of livestock and livestock products to the United States.

The decline in the purchasing power of Western agriculture, combined with rigid costs, brought a sharp curtailment of demand for manufactures from Central Canada. Considerable unemployment emerged in industrial centres. In Nova Scotia, where the high level of activity was heavily dependent upon War requirements, the contraction was particularly severe. At the bottom of the slump the national real income had fallen 14 per cent. During 1921-23 the far-reaching effects of unfavourable foreign influences on the Canadian economy were fully revealed.²

The post-War depression, however, was short-lived. By 1923, notwithstanding the many serious dislocations inherited from the War which had not been overcome, world economic activity had resumed its upward course. Between 1920 and 1926 there was a general and concerted effort to restore the conditions of international exchange as they had existed prior to 1914. Currencies were stabilized on gold, many of the more onerous restrictions on international trade were removed, and international lending was resumed. The reconstruction of devastated areas was quickly accomplished and financially weak countries were bolstered up with international loans. These efforts achieved only a superficial restoration of pre-War trade conditions without bringing a solution to fundamental problems, but they permitted the forces of economic

¹ For example, the settlement of returned soldiers on the land was undertaken at a time of peak prices.

² The extent of the depression in Canada is indicated by the 14 per cent drop (1920 to 1921) in the national real income, the 11 per cent drop in the physical volume of business, the 13 per cent drop in the volume of exports, the 30 per cent drop in the gross value of agricultural production and the increase from 4.9 per cent to 12.7 per cent in the percentage of trade union unemployment. The foreign exchange value of the Canadian dollar during 1921-24 when it moved at an appreciable discount below United States funds and at a premium over sterling—added to the burden of debt charges paid in the United States and put increased pressure on exporters to the United Kingdom, although giving some advantage to domestic producers, and exporters competing with United States interests.

expansion to become effective. The requirements of war had greatly increased productive capacities, particularly in new countries, and stimulated the development of industrial techniques. With the re-establishment of orderly international relations, the new facilities brought an increase in material welfare. By 1925, world production of primary commodities had risen 17 per cent over the 1913 level and the volume of world trade had risen 5 per cent. Canada was quickly affected by the rising tempo of world economic activity.

TABLE 26.—PRICE CHANGES
1913 = 100

	1922	1926	Per cent Change 1926 from 1922	1929	Per cent Change 1929 from 1926
<i>Canadian Selling Prices—</i>					
All Export Prices.....	152	156	+ 3	149	- 4
Wheat.....	140	170	+ 21	152	- 10
Newsprint.....	190	170	- 8	149	- 15
Lumber and Timber.....	190	148	- 7	154	+ 4
Non-ferrous metals.....	99	102	+ 3	101	- 1
<i>Canadian Costs—</i>					
All Import Prices.....	138	137	-	129	- 6
Manufactured Goods Prices.....	155	154	-	144	- 7
Iron and Steel Products.....	152	145	- 4	130	- 6
Railway Freight Rates.....	152	148	- 3	146	- 1
Tramp Shipping Freight ^(a)	130	117	- 10	97	- 18
Interest Rates ^(b)	125	111	- 11	113	+ 2

^(a) Economist Index.

^(b) Yield of Province of Ontario Bonds.

After 1923 the prices of the leading Canadian exports became increasingly favourable in relation to costs.³ These circumstances, together with improved wheat yields, brought a rise of 43 per cent in the value of Canadian exports between 1922 and 1926.

The rising export values which provided the basis for the growing prosperity in Canada in the twenties were due to a number of far-reaching changes which were affecting the Canadian economy during this period. The shortage of food-stuffs in Europe, the application of new techniques to virgin resources for whose products there was a rising world demand, the low cost of ocean transportation resulting from the excess capacity in shipping, and the opening of the Panama Canal, launched a new era of expansion in Canada.

³ By 1926 the average of the prices of all exports of wheat, newsprint, and lumber were 59, 70, 76 and 48 per cent respectively, above those of 1913, compared with increases of 37, 54, 46 and 48 per cent respectively, in the prices of all imports, manufactures, iron and steel and railway freight rates.

Continued Rise in Wheat Exports—increasing dependence of Prairie agriculture on temporary markets

Canadian wheat production had expanded rapidly in response to the new European demands created by the War. These demands were not immediately abated with the renewal of peace. The devastation and dislocations caused by the struggle, agrarian reforms and the Russian revolution prevented the immediate attainment of the pre-War levels of production. The overseas exporting countries, particularly Canada, were called upon to supply the deficiency.

TABLE 27.—WORLD (EXCLUDING CHINA) WHEAT PRODUCTION
(Millions of Bushels)

Annual Averages	25 European Countries	Russia	Canada	United States	Argentina and Australia	All Other	Total
1909-13...	1,355	757	112	652	238	665	3,609
1922-25...	1,197	521	383	779	235	614	3,629
1926-29...	1,340	797	440	661	397	649	4,484

For a few years after the War, European tariff restrictions against the imports of wheat were considerably lower than they were prior to 1914. This liberal policy arising out of the condition of scarcity, and the foreign exchange made available by United States lending, created an expanding market for wheat, of which Canada obtained a growing share, at profitable prices. During 1922-26 Canada supplied 38 per cent of the world's wheat exports, compared with 12 per cent during 1909-14.

TABLE 28.—NET EXPORTS AND IMPORTS OF WHEAT AND FLOUR
(Millions of Bushels)

Averages Crop Years	NET EXPORTS				NET IMPORTS	
	World Total	Six European Exporters	Russia	Canada	France, Italy and Germany	Other European Importers
1909-10 to 1913-14.....	686	114	164	86	164	338
1922-23 to 1925-26.....	759	34	9	268	188	394
1926-27 to 1929-30.....	810	44	14	304	203	441

After 1925 however, the favourable circumstances in the export wheat market began to disappear; 1925 was the first year in which European production exceeded the pre-War levels. It was the year in which Germany regained her freedom

to impose customs duties and thereupon re-enacted high tariffs on foodstuffs. In 1925 Italy began the "battle of the grain" and Austria and Czechoslovakia imposed sliding scale duties on imported wheat. Between 1925 and 1929 the increasing European protection against foodstuffs arising out of the desire for self-sufficiency and the growing industrialism of new countries, together with the continued expansion of European production which was, at least in part, a "spontaneous recovery" from the effects of the War, greatly weakened the international wheat situation. For some time, however, the effects of these basic changes were obscured. The failure of Russia to re-enter the export market on any substantial scale, large United States loans to Europe, speculative holding of surplus stocks, and the high rate of business activity enabled overseas exporters to ship an increasing volume of wheat until the end of the boom in 1929. Wheat prices remained at profitable levels although they had been sagging since 1925. With the satisfactory prices and high yields of 1926-28 Prairie agriculture was prosperous and resumed a rapid rate of expansion. Thus there were serious underlying weaknesses at a time when Canada became even more deeply committed to the profitable sale of wheat which continued to make up nearly a third of her total exports.

The Investment Boom—large investment in transportation facilities and development of northern resources; effects of hydro-electric power, improved mining techniques and the gasoline engine

While the expanding market for wheat was a major factor in the economic growth of Canada during the twenties, other forces were perhaps more important. Prior to 1914 the basic elements of industrialism were steam power, coal and iron. The War and post-War development of hydro-electric power, the gasoline engine, and the use of new industrial metals shifted the balance of industrial advantage. These technological changes were of immense significance to Canada, first, because they brought into economical exploitation large virgin resources, and second, because they decreased the handicaps suffered under the old techniques. The resources of British Columbia and of the northern areas of Ontario and Quebec became the basis of large staple industries. In addition to the agricultural frontier on the prairies, Canada acquired new frontiers on the Pre-Cam-

brian Shield.⁴ The exports of pulp and paper and non-ferrous metals rose to 30 per cent of total exports in 1929 compared with 19 per cent in 1920.

The expansionary effect of these rapidly growing industries, however, was due not so much to the new export incomes which they created, as to the heavy capital expenditures which accompanied their development.

TABLE 29.—CAPITAL INVESTMENT
(Millions of Dollars)

	Total to 1920	Total to 1930	Net New Investment during 1929-30
Primary Industry—			
Agriculture—buildings, implements and livestock.....	2,884 ^(b)	2,817	- 67
Mining ^(c)	560 ^(b)	887	+ 327
Pulp and Paper.....	248	704 ^a	+ 356
Sawmills.....	200	181	- 19
Fishing ^(c)	50	64	+ 14
Sub-Total.....	4,042	4,653	+ 611
Manufacturing.....	2,188	2,868	+ 680
Central Electric Stations.....	448	1,138	+ 690
Transportation and Communication—			
Steam Railways ^(c)	2,635 ^(a)	3,330	+ 695
Canals and River Improvements ^(c) , Harbours, Harbour Improvements, Docks and Terminals—Dominion Expenditure and Guarantees ^(d)	168 ^(b)	280	+ 112
Electric Railways.....	107	231	+ 124
Telephones.....	170	224	+ 54
Highways—Provinces ^(e)	145	310	+ 174
Highways and Streets—Municipalities ^(e)	118 ^(b)	387	+ 269
Sub-Total.....	240 ^(b)	350	+ 110
Public Buildings and Municipal Works ^(f)	3,588	5,121	+1,533
Public Buildings and Municipal Works ^(f)	522 ^(b)	801	+ 279
GRAND TOTAL.....	10,798	14,581	+3,783
Residential Building ^(g)	—	—	+1,062

^(a) Excludes ore reserves or other unmined material. Includes non-ferrous metal smelting and refining.

^(b) 1921.

^(c) Includes fish canning and curing establishments.

^(d) Capital invested in Road and Equipment.

^(e) Estimated.

^(f) Public Accounts Inquiry, Royal Commission on Dominion-Provincial Relations.

^(g) Construction Contracts awarded, MacLean Building Reports, Ltd.

In Canada, as elsewhere, the rising economic activity of the twenties was dependent upon a high rate of investment. The expansion of Western agriculture and the growth of the new staple industries on the new northern frontiers required a heavy expenditure on fixed equipment. The northward extension of wheat growing on the prairies required

a substantial increase in costly transportation facilities. New branch lines were built, main lines improved and canals and harbours enlarged in accordance with the national policy of all-Canadian transportation. In response to the new demands, the requirements of national policies and the optimistic outlook on the future, the railways engaged in unwise competition and invested during 1920-29 nearly \$700 million in road and equipment and a further \$150 million in hotels, telegraphs, and steamships. During the same period the Dominion spent \$236 million on waterways and harbours.

The improved technical facilities and new demands, which opened up the natural wealth of the Pre-Cambrian Shield, involved a particularly heavy investment of capital. The large fixed equipment represented by central electric stations, pulp and paper factories, smelters and metal refineries was the major factor in the exploitation of these resources. The expenditure of nearly \$1,400 million on the construction of such equipment during the decade of the twenties contributed greatly to the prosperity of the period.

Another technical innovation which called for large capital outlays in the post-War years was the automobile. It gave rise to new automobile factories, petroleum refineries, service stations, repair shops and, what was most important, a greatly extended and improved system of highways and streets. The last two items alone involved an investment of some \$380 million during this period.

The heavy capital expenditures involved in the development of the primary industries and transportation stimulated investment in manufacturing, in distribution facilities, in community equipment and housing. During 1920-30 the amount invested in all forms of capital goods reached a total of at least \$6 billion. Near the end of the period, the amount of construction far exceeded the levels attained at the height of the pre-War boom. The amount of foreign capital which came in during the twenties was, however, much smaller than that which was associated with the expansion prior to 1914. Between 1920 and 1924 capital imports were substantial but in 1925, 1927, and 1928 there were net capital exports. During the decade net long-term capital imports were between \$800 million and \$900 million, of which about two-thirds came from the United States. The investment boom of the twenties was very largely financed out of Canadian savings.

⁴ Between 1920 and 1929, the developed water power in Canada rose from 2.6 million horse power to 5.7 million horse power, the gross value of production of pulp and paper (which was closely dependent upon electric power) rose from \$151 million (1921) to \$244 million and the value of production of non-ferrous metals rose from \$76 million to \$154 million.

The increase in export incomes resulting from the expansion of Western agriculture and the exploitation of hitherto unused resources by the application of improved techniques, together with the heavy capital expenditures which arose out of these developments, brought rising prosperity and a very substantial improvement in material welfare. The average per capita real income rose by fully one-third during the decade.

TABLE 30.—INDICES OF CANADIAN ECONOMIC PROGRESS, 1920-29
1920 = 100

—	Population	Real National Income	Physical Volume of Business	Volume of Exports	Efficiency of Production in Manufacturing	Index of Real Wages
	(a)	(b)	(c)	(d)	(e)	(f)
1920.....	100	100	100	100	100	100
1922.....	104	100	106	118	130	116
1925.....	110	126	133	161	142	114
1925-29 average	116	148	162	172	146	120

(a) Estimates of the population by the Dominion Bureau of Statistics.

(b) Computed from estimates of the national income by the Dominion Bureau of Statistics for 1920-26 and from the Bank of Nova Scotia estimates for 1926-29. The index of the real national income was computed by dividing the indices of the national money income by the Dominion Bureau of Statistics index of the cost of living.

(c) Dominion Bureau of Statistics Index.

(d) Index of the value of exports divided by the Dominion Bureau of Statistics index of export prices.

(e) Volume of manufacturing production per employee, *Canada Year Book*, 1934-35, p. 490.

(f) Dominion Department of Labour index of wages divided by the Dominion Bureau of Statistics index of cost of living.

Maritime Provinces—foreign markets and technological changes unfavourable; prolonged post-War depression and federal assistance.

The external forces and the technological changes of the 1920's, while favourable to Canada as a whole, were adverse to the Maritime Provinces. During the thirty years prior to the War, the decline of the old techniques destroyed the prosperity based upon the sailing ship and the sea, while the rise of coal, iron and the railway brought a growing dependence upon the continental interior. The development of the coal and steel industries which resulted from the "wheat boom" and the national policies provided alternatives to the declining occupations. In this manner, parts of the Maritimes had participated in the great expansion of 1896-1913. The post-War expansion, however, which was not so much associated with railway building as with the rise of new sources of power (electricity and oil) and the newer industrial metals, passed them by. As in the former period,

the long-term trend in their foreign markets was downward. Under such circumstances, the depression which set in during 1921 continued in these provinces long after it had been overcome and expansion renewed elsewhere. In this decade they made virtually no progress.

TABLE 31.—THE ECONOMIC PROGRESS OF THE MARITIMES, 1920-29

Indices 1920=100

—	Population		Capital Invested ^(a)		Net Value of Production ^(b)		Average per Capita Income ^(c)	
	Maritimes	Canada	Maritimes	Canada	Maritimes	Canada	Maritimes	Canada
							\$	\$
1920...	100	100	100	100	100	100	—	—
1925...	101	110	96	116	74	99	269	439
1929...	102	117	109	138	74	107	313	470

(a) Total capital invested in the primary industries (agriculture, mining, fishing and forestry), manufacturing, central electric stations, and provincial and municipal public works.

(b) Net value of "goods" production.

(c) Calculated from the estimates of national income prepared by the Research Staff of the Commission.

Between 1920 and 1929 the populations of Nova Scotia and Prince Edward Island remained practically stationary while that of New Brunswick rose but slightly, compared with an increase of 18 per cent in the two Central Provinces. During the decade, there was a considerable emigration to the United States. In none of the years of the period 1921-29 did the net value of (goods) production in the Maritimes approach the high figure of 1920, whereas, in each of the other provinces of the Dominion, it had been surpassed by 1928.

The War had been a powerful stimulus to the Maritime economy. The cessation of the exports of dried fish from Europe, the heavy demand for West Indian sugar, and the growth of the fresh fish trade to Central Canada greatly extended the markets of the fishing industry. The demand of the munitions industries for iron and steel, the shipbuilding orders of the Canadian and Allied Governments, the high prices for lumber and the decline of the competition of other regions with local agriculture, brought prosperity to the other principal industries. The Halifax disaster brought about a temporary building boom. At the beginning of the post-War depression, all these favourable influences disappeared suddenly and simultaneously.

During the War Brazil, Porto Rico, Cuba, and the British West Indies drew virtually the whole of their supplies of dried fish from Nova Scotia and Newfoundland. The high meat prices and the

Government transportation subventions brought a large increase in the sales of fresh fish to Quebec and Ontario. The removal (as a War measure, in 1918) of the shipping restrictions which had partially nullified, for the Maritimes, the Underwood Tariff of 1913 permitting free entry of fresh and frozen fish into the United States, gave the fishing industry profitable access to the markets of that country. These advantageous circumstances, however, quickly disappeared. After 1920 production of dried cod from competing sources increased rapidly. European importing countries became self-sufficient behind tariff walls. Government subsidies and technological improvements enabled Norway and Iceland to increase production greatly and to capture important markets. The steep decline in sugar prices sharply curtailed the purchasing power of the principal consumers in the West Indies. Finally, dried cod was being gradually replaced as an article of diet by other foodstuffs. The fresh fish trade grew but slowly. In 1919 the subventions for the transportation of fresh fish to Central Canada were stopped. In 1921 the United States Government withdrew the War-time privileges accorded to Canadian fishing vessels and reimposed tariffs (which were increased in 1922) on fresh and frozen fish. Confronted with such an array of obstacles, Nova Scotia's highly important fishing industry declined.

TABLE 32.—INDICES OF PRICES AND THE VALUE OF FISH PRODUCTION IN THE MARITIMES

—	Prices of Dry Shore Codfish at Halifax	All Wholesale Prices	Cost of Living	Total Value of Fish Production Maritime Provinces
1913.....	100	100	100	100
1918-20 average.....	192	217	168	152
1921-25 ".....	118	159	155	112
1926-29 ".....	109	152	152	130

The resources hitherto employed in the fisheries sought opportunities elsewhere. Some owners of fishing vessels turned to rum-running for a new source of income. Despite the fact that alternative employments were few and the problems of readjustment difficult, the number of persons employed in the fishing industry in Nova Scotia declined from 26,000 in 1919 to 20,000 in 1929.

Lumbering, the principal industry in New Brunswick and an important one in Nova Scotia, faced growing difficulties during the twenties. The

depression in British building restricted the sales in the English market while the opening of the Panama Canal and low ocean freight rates intensified competition in the Eastern United States and Canada. During 1921-29 the production of lumber in New Brunswick never recovered the pre-War peak of 1911 and remained far below the levels of the War years. The average annual output in Nova Scotia in this decade was less than half of what it had been during 1908-14. The depressed conditions in lumbering encouraged the utilization of forest resources for the manufacture of pulp and paper. Between 1920 and 1929 the production of pulpwood in the two Provinces was doubled. The manufacture of paper, however, was slow in getting under way. It began in 1923 in New Brunswick but not until 1930 in Nova Scotia. Despite this development the total net value of forestry production in the Maritimes for 1929 was less than for 1922.

The rise of the Nova Scotia iron and steel industry was directly linked with the railway expansion of the "wheat boom." In the post-War period the demand shifted from steel rails and other heavy forms to lighter materials and structural steels such as are used in motor-car manufacturing and building construction. The Nova Scotia industry was at a disadvantage compared with that in Central Canada which was closer to the market, had access to larger supplies of scrap metal, and whose competitive position was improved by the disproportionate War-time increases in freight rates from the Maritimes. In Ontario the production of pig-iron in 1928 and 1929 far exceeded the levels reached during 1916-20, but in Nova Scotia output remained considerably below both the immediate pre-War and War-time peaks. In 1913 Nova Scotia produced 43 per cent of Canada's pig-iron; in 1929 this ratio had fallen to 29 per cent.

Coal mining suffered at once as a result of the difficulties of the iron and steel industry.⁵ Furthermore, the market in Central Canada, which took one-third of the output in 1913, was lost during the War. The recovery of this market was assisted by the 20 per cent reduction in Maritime freight rates in 1927 and the federal subventions for the transportation of coal to Ontario and Quebec which were established in 1928. With these rail freight reductions and the low water rates which prevailed during this period, the Central Canadian market was more than recovered by 1929. A further attempt was made to help the industry by the

⁵The consumption of coal in Nova Scotia (used very largely by the iron and steel industry) was 2.9 million tons in 1913 and 1920 but less than 2.2 million tons in 1929.

offer of federal bonuses (started in 1927) to gas and coking plants using Canadian coal. These various methods of assistance were in part responsible for a considerable revival of production but in 1929 the total was still 12 per cent below the output of 1913.

The relative, and in some cases absolute, decline in Maritime manufacturing which began at the end of the last century continued during the twenties. The disadvantages of these Provinces arising out of their isolation from the large markets of Central Canada and the West, their distance from the industrial centre of gravity of the continent situated in the Mid-Western United States, the unfavourable circumstances affecting the local exporting industries, and the adverse railway freight rate situation (as compared with pre-War levels) prevented them from sharing in the expansion of manufacturing which took place in Ontario and Quebec. They were unable to benefit from the new developments which stimulated the remarkable growth in the lighter industries, in the production of packaged consumers' goods, new textiles and durable consumers' goods such as motor cars, radios, electrical appliances and other household furnishings. However, some progress was made in the processing of local natural products and also of certain imported raw materials such as sugar and oil. A number of specialty manufacturers held their position, the most important being specialty textiles, shoes and candies. Nevertheless, manufacturing in the Maritimes declined during this period. In 1929 employment in manufacturing was greater than in 1920 in every province except Nova Scotia and New Brunswick. For Canada as a whole, manufacturing employment during the decade rose 14 per cent but fell 6 per cent in the Maritime Provinces.

With the disappearance of War-time demands and prices, the competition of other regions with Maritime agriculture was intensified. Consequently, the acreage devoted to field crops decreased steadily (there was a small rise in Prince Edward Island) during the twenties. However, there was some progress in the production of dairy products for the sheltered local market and of agricultural export specialties,⁶ although circumstances were not favourable. The Nova Scotia apple industry encountered increasing difficulties with diseases and pests and was confronted in the depressed English market with stiffer competition from British Columbia and a better graded product from the United

States. During the War and the immediate post-War years, valuable markets for potatoes were built up in the United States and Cuba. The Underwood Tariff of 1913 had admitted potatoes free subject to a small countervailing duty. In 1921 the United States potato tariffs were re-imposed and, in 1922, raised to 30 cents per bushel. The Cuban market became less attractive as the sugar prosperity disappeared, and in 1927 tariffs were sharply raised. However, the great progress in the development of seed potatoes in Prince Edward Island and New Brunswick kept them in the market despite tariffs and depressed conditions. In the face of the many unfavourable factors, Maritime agriculture failed to prosper. The number of gainfully occupied engaged in the industry fell slightly during the decade.

The difficulties of the widespread economic readjustment which the Maritime region had to undergo during the twenties were enhanced, particularly during the first half of the period, by the effects of the national policies. The isolation of these Provinces from the markets of the rest of Canada was intensified by the War and immediate post-War rise in freight rates. In the Maritimes these rates had risen approximately 20 per cent more than in Ontario and Quebec. The policy of protective tariffs, although it was not altered in any important respect, bore with increasing weight upon the depressed and marginal exporting industries. However, during the latter part of the decade, the national policies were somewhat modified so as to apply more favourably to this region. In 1927, following upon the recommendation of the Duncan Commission, the railway rates within the territory east of Levis and Diamond Junction, and on traffic moving westward out of this territory were reduced 20 per cent. Thus the pre-War relationship between Central Canadian and Maritime rates was restored.

The changes in the tariff and trade regulations did not significantly alter the general level of protection, but a number of new provisions were adopted which were calculated to increase traffic through Maritime ports. In 1923 a reduction of 10 per cent on preferential rates in excess of 15 per cent was granted where imports were shipped direct to Canadian ports. In 1926 the application of all preferential rates was made dependent upon direct shipment to Canadian ports. A new Canada-West Indies Trade Agreement providing for reciprocal preferences became effective in 1927. Although the effects of this Agreement upon exports were disappointing to the Maritimes, the establishment of a

⁶ These were silver forces in Prince Edward Island, potatoes in Prince Edward Island and New Brunswick, and apples in Nova Scotia.

regular and adequate steamship service to the West Indies subsidized by the Dominion yielded distinct benefits. These modifications in the national transportation and tariff policies, the Dominion subventions to coal, large Dominion expenditures (by direct outlays and guarantees) for the improvement of the harbours of Halifax and Saint John, together with the sharp rise in economic activity in Canada and elsewhere, brought a substantial recovery to this region during the latter part of the decade. Between 1926 and 1929 the total income of these Provinces rose slightly more rapidly than that of the rest of the country. By 1929 some of the unfavourable circumstances had disappeared and the major readjustments required by the remainder had been accomplished. At the end of the period, the Maritimes had less of the feverish activity of a boom than other parts of Canada but they were better prepared to withstand the shock of the depression.

Prairie Provinces—renewed expansion following recovery of wheat prices; diversification in Manitoba and increasing dependence upon wheat in Saskatchewan and Alberta.

The collapse of wheat prices after 1920 coupled with rigid costs placed a severe strain on Western agriculture.

TABLE 33.—THE PRICE OF WHEAT AS PERCENTAGES OF CERTAIN FARM COSTS, 1913-25

	Manu- factured Goods	Farm Cost of Living	Wages of Farm Help
1913.....	100	100	100
1920.....	118	135	104
1921.....	104	111	86
1922.....	90	93	76
1923.....	77	81	69
1924.....	92	97	80
1925.....	116	126	103

The decline in agricultural income was intensified by poor yields, and by the fall in cattle prices to which the United States' tariffs of 1921 and 1922 contributed. The difficulties of the Western farmer found expression in the agitation for the re-establishment of the Wheat Board, in the growth of farmers' organizations, and finally in the establishment of the voluntary wheat pools during 1923 and 1924. The Provincial Governments of Manitoba and Saskatchewan endeavoured to relieve the situation by making available agricultural credit at lower than open market rates, and Alberta by heavy expenditures for irrigation and advances for seed grain, purchase of live stock, etc.

During the depressed farm conditions of 1921-24 economic expansion in the Prairie Provinces virtually ceased. In this period, however, certain important readjustments were made. A reduction of 7.5 cents per bushel in the freight rates on wheat (Regina to Fort William) was effected in 1922 by the re-establishment of the Crow's Nest Pass Agreement rates on grain and flour moving eastward from the Prairies. A large area of the wheat-growing region was enabled to benefit from the opening of the Panama Canal by the decreases of 20 per cent in 1922 and a further 10 per cent in 1923 on grain rates from Prairie points to the Pacific coast. Between 1920 and 1924 the total cost of shipping wheat from Regina to Liverpool fell from 67 cents per bushel to 33 cents per bushel. In this period also, the national policy of protective tariffs was somewhat modified in the direction of reducing the costs of the primary producer. The War-time increases in the tariff (7½ per cent on the general and intermediate rates and 5 per cent on the preferential rates) were abolished in 1919 and 1920. In 1919, 1920 and 1924 substantial reductions were made in the duties on farm machinery. In 1924 the general and intermediate rates on tillage implements stood at 7½ per cent compared with 17½ per cent and 20 per cent under the 1907 tariff. The reduction of costs and the sharp recovery of wheat and livestock prices in 1924 and 1925 opened a period of renewed expansion on the Prairies.

TABLE 34.—THE PRICE OF WHEAT AS PERCENTAGES OF CERTAIN FARM COSTS, 1913-29

	Manu- factured Goods	Farm Cost of Living	Wages of Farm Help
	1913 = 100	1913 = 100	1913 = 100
1924.....	92	97	80
1925.....	116	126	103
1926.....	110	117	92
1927.....	113	116	89
1928.....	104	107	81
1929.....	106	109	81

The relation of wheat prices to costs was favourable and yields were abnormally high. The Prairies once more became a magnet for immigrants. In the occupied areas, the improved acreage was rapidly increased and another wave of frontier settlement spread out over northern Alberta and Saskatchewan. The northward thrust of settlement was encouraged by the development of new early maturing wheats and the extensive provision of railway facilities. Between 1926 and 1931 the

occupied acreage rose 24 per cent and the improved acreage 21 per cent. Agricultural prosperity and frontier expansion in Western Canada operating within the framework of the national policies once more set in motion the stimuli to the national economy made familiar by the "wheat boom". The construction of railroads, the building of towns and villages, the growth of cities and the provision of community facilities brought a high rate of economic activity to the region and gave a strong impetus to production in Eastern Canada and British Columbia. Between 1920 and 1930 railway mileage in the three Provinces increased by nearly 2,900 miles,⁷ compared with virtually no increase in the remainder of Canada. By the end of 1930 practically every part of the area of the Prairies on which agriculture is feasible had been brought within 10 miles of the railway. Also, in response to regional pressure, a new transportation outlet (the Hudson Bay Railway) for grain was constructed at a cost to the Dominion of \$50 million.

At the close of this decade the settlement of the Western plains was virtually completed, and the area was provided with the capital equipment and the community facilities adequate for a high standard of living. The great national purposes, which led to the acquisition of the Northwest and to the attempt to build a transcontinental economy on the basis of the settlement and the economic growth of this empire, were now fulfilled.

While the same broad forces played upon each of the provinces during the twenties, there were significant differences in the nature of their development.

TABLE 35.—AGRICULTURAL EXPANSION IN EACH OF THE PRAIRIE PROVINCES, 1920-30
Indices 1920 = 100

	Manitoba		Saskatchewan		Alberta	
	1920	1930	1920	1930	1920	1930
Population.....	100	116	100	124	100	125
Area of Occupied land.....	100	104	100	126	100	133
Area of Improved land.....	100	106	100	124	100	151
Percentage of Area of Field Crops in Wheat.....	45	36	58	63	49	57
Percentage of Urban to Total Population	43	45	29	32	38	38
Percentage of Number Engaged in Agriculture to Total Gainfully Occupied.....	40	35	65	60	53	51

⁷ Of this mileage, 1,600 miles were added in Saskatchewan, 1,300 in Alberta and 100 in Manitoba.

In Alberta and Saskatchewan, where land for frontier settlement was still available, expansion was much more rapid than in Manitoba. The economic growth in the latter Province was largely confined to the westward extension of the hydro-electric, pulp and paper and mining development of Ontario and Quebec. The application of new and improved techniques to the resources of the Pre-Cambrian Shield which crosses northern Manitoba was a replica, on a much smaller scale, of what was taking place in Central Canada. Between 1920 and 1930 the developed water power in Manitoba increased from 85,000 horse power to 312,000 horse power. The manufacture of paper began in 1927. Gold output became significant in 1928. The production of zinc-copper-silver in the Flin Flon area did not get under way until 1930, but the capital expenditures in connection therewith were made during the latter part of the twenties.

These and other developments introduced an important element of diversity into Manitoba's economy. The net value of production of mining, forestry and electric power rose from 5 per cent of the total in 1920 to 12 per cent in 1930. Considerable progress was also made in manufacturing and the contribution of this industry to the total net value of (goods) production increased substantially. The dependence upon agriculture declined and agriculture itself became less dependent upon wheat. The percentage of the area of field crops in wheat was 45 per cent in 1920 but only 36 per cent in 1930. The farm income from feed grains, live stock and dairy products now surpassed that obtained from wheat. Manitoba had attained an important degree of maturity and had come a long way from the pioneer stage with its overwhelming reliance upon a single staple. However, the metropolitan area of Winnipeg continued to be heavily dependent upon the wheat economy of Saskatchewan and Alberta.

The economic growth of Saskatchewan and Alberta during this decade was due almost entirely to the expansion in the production of wheat. There was some development of oil in Alberta but the coal mining industry lagged. The importance of this one grain was partly the result of the relatively greater rise in the price of wheat than in the prices of live stock and dairy products, and partly, the result of the rapid mechanization of farms which displaced a large acreage of feed grains.⁸

⁸ The increase from 38,000 to 62,000 in the number of tractors, from 73,000 to 135,000 in the number of motor cars and trucks and from practically nil to 9,000 in the number of combines on farms in the Prairie Provinces between 1921 and 1931 shows how the horse was being displaced by mechanical power.

During 1926-28, 81 and 70 per cent respectively of the total cash receipts from the sale of farm products in Saskatchewan and Alberta came from wheat, compared with but 43 per cent in Manitoba. In the same period, the two former Provinces derived 62 and 50 per cent of their total incomes *directly* from agriculture while in Manitoba this percentage was only 25 per cent. The prosperity of Saskatchewan and Alberta was almost completely dependent upon the production of a single commodity of which the volume of production was determined by the extreme variations of a hazardous climate and which was sold on a precarious foreign market.

British Columbia—rapid economic expansion; the stimulus from the opening of the Panama Canal, low ocean freight rates and rising demand for non-ferrous metals

The rate of economic growth of British Columbia during this decade exceeded that of any other Canadian region or province.

TABLE 36.—THE ECONOMIC PROGRESS OF
BRITISH COLUMBIA, 1920-29

INDEXES 1920=100

	Population		Capital Invested ^(a)		Net Value of Production ^(b)		Per Capite Income ^(c)	
	British Columbia	Canada	British Columbia	Canada	British Columbia	Canada	British Columbia	Canada
1920...	100	100	100	100	100	100	\$ —	\$ —
1926...	130	116	323	116	126	99	554	432
1929...	130	117	165	120	145	107	600	470

(a) Total capital invested in the primary industries (agriculture, mining, fishing and forestry), manufacturing, central electric stations, and provincial and municipal public works.

(b) Net value of "goods" production.

(c) Calculated from the estimates of national income prepared by the Research Staff of the Commission.

The development of the new sources of power (electricity and oil), the rise of the new industrial metals, and the growing demand for wood-pulp and paper suddenly brought a large heritage of natural resources within the range of economic exploitation. The opening of the Panama Canal and the abnormally low ocean freight rates immensely improved British Columbia's general competitive position, and in particular opened large international markets to her bulky exports. The improved techniques and greatly cheapened transportation produced a rate of economic expansion in British Columbia during the twenties equalled by few other areas in the world.

The problems of treating the complex non-ferrous metal ores of the Kootenay district were largely solved during the War, but production in any great

volume was not attained until the post-War period. Between 1920 and 1929 the output of copper more than doubled, of silver increased by three times, of zinc by over four times, and of lead by nearly ten times. In 1930 British Columbia produced nearly one-tenth of the total world production of lead and zinc. The production of pulp and paper which had begun before the War expanded considerably during the twenties in response to demand from the United States Pacific Coast and the Orient. Both mining and pulp and paper were closely related to the availability of hydro-electric power. In 1929 the developed water power per capita in British Columbia was higher than that in any other province.

The opening of the Panama Canal was an event of first importance to the leading industry on the Pacific coast, lumbering. Prior to the War, the high cost of transportation practically excluded British Columbia lumber from foreign markets and less than one-fifth of the output was exported. The industry was almost entirely dependent upon sales in the Prairie Provinces. In 1920 (when the Panama Canal was not yet in full operation) the cost of shipment of Pacific coast lumber to New York was \$27.30 per thousand feet. In 1929 this cost had fallen to \$10.11.⁹ During this period, the output of British Columbia lumber was almost doubled. About one-half of this increased production was exported, over 60 per cent of the exports going to the United States where lumber had had free entry since 1913. The significance of the Panama Canal to British Columbia and also to the lumber industry in Eastern Canada is further illustrated by the fact that nearly one-fourth of all the sales of lumber in 1929 from the former Province consisted of water-borne shipments to the Atlantic Coast of North America.

One of the most important results of the favourable circumstances which promoted a rapid expansion of the primary industries was the capital expenditures to which they gave rise. Much of the exceptional prosperity during this period had its basis in the large investment of capital. During the twenties the volume of new construction in British Columbia was nearly equal to that in the three Prairie Provinces combined.

Prior to the War British Columbia was closely dependent upon the transcontinental Canadian economy and the national transportation and

⁹The great importance of this decrease in transportation charges and its revolutionary effects upon the industry are indicated by the comparison of this decline with the total mill cost of British Columbia lumber of \$22.50 per thousand feet in 1920.

developmental policies.¹⁰ During the post-War period this dependence upon Canadian markets and policies declined. In the twenties the primary industries expanded almost entirely in relation to foreign demands. About half the lumber, virtually the whole of the mineral production, nearly all of the fish, and a large part of the apples were sold in external markets. British Columbia continued to be deeply affected by the national policies but she derived her income mainly from sales abroad.

The modifications in the national transportation policy during the twenties, however, enabled her to benefit extensively from her improved position. The Panama Canal greatly extended the potential hinterland of the port of Vancouver. The freight rate reductions on grain in 1922, 1923, 1925 and 1927 increased the area in Alberta and Saskatchewan from which wheat could be profitably shipped via the Pacific coast. The large program of railway branch lines speeded up the development of areas tributary to Vancouver.¹¹ Of considerable importance, also, was the regional equalization of railway freight rates that took place during the post-War decade.¹² These rate reductions, together with the opening of the Panama Canal and the rapid growth of the local exporting industries, were particularly helpful to Vancouver which grew to become the third largest metropolitan centre in Canada. During 1921-31 its population rose by over 50 per cent. The capital expenditures involved in this expansion contributed greatly to prosperity of the Pacific coast region.

Central Provinces—technological changes and favourable foreign markets induce rapid development of forest and mineral resources; increasing industrial and financial concentration in this region.

The economic developments of this decade were highly favourable to Ontario and Quebec. Agricultural expansion in the Prairie Provinces and the rapid growth of the exporting industries in British Columbia within the framework of the national

policies widened the opportunities of the commercial and industrial enterprises concentrated in the central region. The progress of this area along the old lines was greatly supplemented by the rise of their own new frontiers and by new direct external contacts which resulted from the application of improved techniques to the resources of the Pre-Cambrian Shield. Ontario and Quebec recovered quickly from the 1921 depression and thereafter enjoyed increasing prosperity until 1930.

TABLE 37.—THE ECONOMIC PROGRESS OF ONTARIO AND QUEBEC, 1920-29
Indices 1920=100

	Population		Capital Invested ^(a)		Net Value of Production ^(b)		Per Capita Income ^(c)	
	Ontario and Quebec	Canada	Ontario and Quebec	Canada	Ontario and Quebec	Canada	Ontario and Quebec	Canada
1920...	100	100	100	100	100	100	0	0
1926...	118	110	118	116	96	99	480	453
1929...	118	117	143	138	118	107	485	470

^(a) Total capital invested in the primary industries (agriculture, mining, fishing and forestry), manufacturing, central electric stations, and provincial and municipal public works.

^(b) Net value of "goods" production.

^(c) Calculated from the estimates of national income prepared by the Research Staff of the Commission.

Prior to the War the economic growth of the Central Provinces was closely dependent upon their ability to sell manufactured goods and services to the exporting industries in the other regions of Canada, principally the Prairie West. The foreign outlets for their products had become of minor importance. It is true that the attack on the Pre-Cambrian Shield began before 1914, but large-scale developments had to await the new conditions of the War and post-War periods. The lack of coal and iron ore was a serious obstacle in the age of steam and steel. The development of electricity, the gasoline engine and the rising demand for the newer industrial metals now greatly shifted the position of comparative advantage. These changes, together with the improvements in metallurgical processes and the increasing consumption of pulp and paper brought the resources of northern Ontario and Quebec into their own.

Aside from the existence of mineral deposits and unexploited timber resources, the central factor in the new developments was the availability of hydro-electric power.¹³ Because of the interior location of Canada's mineral resources and the low grade

¹⁰ Seventy per cent of her total production of lumber was sold in the booming markets of the Prairie Provinces.

¹¹ Between 1921-22 and 1929-29 the shipments of wheat to Europe through this port rose from 4.5 million bushels to 61.1 million bushels.

¹² This may be illustrated by a comparison of Fifth Class Maximum Standard Mileage Rates for a distance of 400 miles. (This class and distance is selected merely to show the direction of the changes.) In 1914, Pacific rates were 77 per cent; Saskatchewan-Alberta rates 49 per cent; and Manitoba rates 37 per cent above those of Ontario and Quebec (Central rates). In 1923, Pacific rates were only 32 per cent and Prairie rates 14 per cent above the Central rates. In 1922, the Pacific Standard rates were lowered from a level 1½ times the Prairie rates to a level 1¼ times the Prairie rates.

¹³ Its great importance is indicated by the fact that approximately 100 horse power of energy are required per ton of daily output of newspaper.

character of many of the ores, economic exploitation would not be practical were it not for the availability of cheap electric power with which to mine and to treat the ores on the spot. Between 1920 and 1930 the developed water power in Ontario and Quebec rose from 2.0 million horse power to 4.8 million horse power. In the latter year, nearly 30 per cent of this power was utilized by the pulp and paper industry and 12 to 15 per cent by the mining and metallurgical industries. The production of hydro-electric energy in the two Central Provinces during 1930 was equivalent to approximately 13 million tons of coal, or about twice the total annual average output of coal in Nova Scotia.

The abundance of cheap hydro-electric power and the favourable markets for wood-pulp, paper and non-ferrous metals were the bases of the rapid expansion in the exploitation of the resources of the northern areas. During this decade, the production of non-ferrous metals in the Central Provinces was almost doubled and the output of paper increased by nearly three times.¹⁴ The manufacturing of pulp and paper became Canada's leading manufacturing industry and newsprint paper the second largest Canadian export. In 1930 the net value of production in mining, forestry and electric power made up one-fifth of the total net value of (goods) production in the two Provinces. The population of the northern districts, which was almost entirely dependent upon these activities, became about equal to the population of the whole of Alberta.

The development of large exporting industries and the growth of the new communities dependent upon them constituted a significant change in economic structure of the Central Provinces. It lessened relatively the importance of the other regions as markets for the manufactures and services of Ontario and Quebec. Secondly, it was the basis of heavy capital expenditures which added greatly to the prosperity of these Provinces during this period. The rapidly expanding industries which obtained their income from abroad and spent it mainly in the protected domestic market more than took up the slack which resulted from the declining rate of growth (as compared with the pre-War period) of Prairie agriculture. The investment of over one billion dollars in central electric stations, pulp and paper factories and mines during this decade provided ample outlets for activities formerly dependent upon the railway and building boom of Western Canada.

¹⁴ Gold output rose from \$12 million to \$39 million and other non-ferrous metals from \$43 million to \$59 million.

Another technical innovation, which during the twenties brought a large increase in the income of the central region from external sources, was the automobile. This new means of transportation, besides giving rise to important new manufacturing and service industries and to heavy capital expenditures on roads and streets, was the principal factor in the rapidly growing tourist trade from the United States. In 1929, the expenditures of foreign tourists in Canada reached an estimated total of \$300 million, a figure greater than the value of any Canadian commodity export. At least 80 per cent of this amount was spent in Ontario and Quebec.

While the basis of the economy of Central Canada was substantially broadened by the new developments, manufacturing continued to be the predominant activity. This industry received a considerable stimulus from the new export incomes of both this region and Western Canada which the national policy of protective tariffs effectively directed to the domestic producer. Furthermore, Ontario and Quebec were able to benefit most from the technological changes of this decade. The production of automobiles, electrical apparatus and supplies, the new textiles, radios, etc., was confined almost entirely to these Provinces. The concentration of manufacturing in Central Canada became even more complete.

TABLE 38.—PERCENTAGES OF THE NET VALUE OF MANUFACTURES IN ONTARIO AND QUEBEC TO THE CANADIAN TOTALS, 1910-29

	Ontario and Quebec		Ontario	Quebec
	1910	1929	1929	1929
Total Textiles.....	90	91	47	44
Cotton Textiles.....	80	94	21	73
Wool Textiles.....	90	94	80	14
Total Iron and Steel Products.....	81	86	68	20
Primary Iron and Steel.....	—	75	59	19
Agricultural Implements.....	98	98	95	3
Railway Rolling Stock.....	67	76	23	53
Automobiles.....	100	96	96	—
Electrical Apparatus and Supplies.....	90	99	77	22
Chemicals and Chemical Products.....	75	90	59	31
Rubber Products.....	91	99	74	25
Boots and Shoes.....	94	97	36	61
Furniture.....	97	95	76	18
Glass Products.....	73	92	53	38
Tobacco.....	95	100	11	89
Pulp and Paper.....	93	86	32	54
Flour Mills.....	82	58	45	13
Saw-Mills.....	51	38	22	16
Non-ferrous Metal Smelting and Refining.....	—	78	54	23
Fruit and Vegetable Canning.....	98	75	65	10
Meat Products.....	68	66	51	15
Liquors.....	83	81	40	41
Petroleum Refining.....	83	84	41	14
Central Electric Stations.....	63	75	42	33
Total of Listed Manufactures.....	80	84	51	33
All Manufactures.....	80	82	51	31

In Quebec, although considerable progress was made in the processing of natural products with the use of hydro-electric power, manufacturing continued to be mainly dependent upon consumers' goods (clothing, cotton textiles, boots and shoes, tobacco) requiring a large supply of labour. Ontario, on the other hand, specialized in the rapidly growing, mechanized industries producing durable consumers' goods and machinery. For a number of these (automobiles, farm implements and rubber products) important export markets were built up on the basis of Empire preferences, and carefully contrived loopholes in the tariff which gave access to United States techniques, tools and parts.

The concentration of manufacturing in Central Canada was accompanied by an increasing concentration of the financial, commercial and distributive services in this region. The fact that Canada was able to finance a very large part of the post-War capital investment out of its own savings opened large opportunities to Canadian financial institutions. The increasing amount of capital required was gathered together from all over Canada and allocated to investment purposes throughout the entire country by the financial houses and promoters of Montreal and Toronto. Furthermore, the business boom of 1926-29 brought another wave of corporate mergers and consolidations which centralized industrial control and the location of head offices even more completely in the metropolitan centres of Ontario and Quebec. This industrial and financial centralization had the effect of canalizing a very large part of the profits, net incomes, and wealth which arise from activity over the whole country, into the central region. In 1930, 80 per cent of the total net corporate incomes subject to the Dominion corporation income tax and 77 per cent of all individual incomes over \$10,000 subject to Dominion income tax appeared in the two Central Provinces. In the same year, four-fifths of all the dividends from stocks and interest from bonds paid to Canadian individuals were received by residents of Ontario and Quebec.

The growing concentration of manufacturing, commerce, and finance was reflected in the increasing urbanization and the rapid expansion of the metropolitan centres of the two Provinces. Between 1921 and 1931 the urban population rose from 58 per cent to 61 per cent of the total in Ontario, and from 56 per cent to 63 per cent in Quebec. In Ontario agriculture declined relatively, and in Quebec, absolutely. In the latter Province, where the migration from the country to the city was greatest, the number of farms and the area of improved land actually decreased, despite the

encouragement to colonization given by the Provincial Government and the Church. Quebec became the most highly urbanized Province in Canada. The principal urban areas, Montreal and Toronto, which became the metropolitan centres for the entire Canadian economy, increased their populations during this decade by 39 per cent and 33 per cent respectively, compared with an increase of 18 per cent in the population of the country as a whole. Montreal continued to be heavily dependent upon the transcontinental economy established by the "wheat boom" and the national policies, while Toronto became more closely associated with the rapidly expanding industries on the Pre-Cambrian Shield.

*Significant Changes in the Canadian Economy—
rise of new export areas and decline in unifying
influence of wheat; growing vulnerability to
external fluctuations, increasing rigidities and
specialization*

The impact of technological changes and favourable foreign markets upon Canada's undeveloped resources brought, during the twenties, another period of expansion and prosperity. However, the uneven distribution of the resources which were now drawn into exploitation meant that the various Canadian regions were affected very differently. The old economy of the Maritimes languished; good prices (during the latter half of this period) and agricultural settlement of the remaining fringes, produced a considerable, though not a spectacular, expansion in the Prairies; Central Canada and British Columbia surged ahead on the basis of new and rapidly growing export industries. The nature of the development during this decade modified the simple unity of the Canadian economy which rested on the rising production and exportation of wheat. Prior to the War, there was one predominant export area, the Prairie West, whose growth under the influences of the national policies built an integrated transcontinental economy. During the twenties new important export staples emerged in two other regions. Formerly the economy had but a single important external contact; now there were several. One promoted East-West cohesion; the others emphasized North-South relationships and regional economic independence.

The national economic policies were continued without any significant changes. The specific applications of these policies during the twenties

were largely attempts to round out the great national purposes for which they had been adopted. The settlement of the Northwest was virtually completed. The national transportation system was consolidated and improved, and branch lines were added to encourage the development of the few remaining areas of unsettled agricultural land. No new and sweeping projects were launched and the Dominion rested on its past accomplishments. However, with the unequal levels of prosperity, the restrictive effects of the national policies upon certain regions became more burdensome and much dissatisfaction arose. No new policies were initiated but a number of modifications were made in the old for purposes of regional appeasement. The alterations in the tariff consisted mainly of a much greater use of certain devices (drawbacks, special exemptions, etc.) which tended to reduce the costs of the primary producer without changing the general level of protection. The influences of the Dominion on the freight rate structure, as exercised by statute, orders in council and the decisions of the Board of Railway Commissioners, tended to decrease regional differentials. The rising incomes of the twenties made it relatively easy to get acceptance of the adjustments necessary to maintain a national economic integration.

While the circumstances of this decade were favourable to Canadian expansion they also increased the vulnerability of the economy. The new export staples were the result of highly specialized activities. Large areas of the country, where it was either wheat or nothing, pulp and paper or nothing, lumber or nothing, non-ferrous metals or nothing, became dependent upon the exportation of a single or a very few commodities. If the foreign prices of these fell to unprofitable levels there would be no alternative occupations. On the Pre-Cambrian Shield and over a large part of the Prairies self-sufficiency even for a bare subsistence would be impossible. The principal products consisted of raw materials, and hence the probability of extreme fluctuations was great. In a number of cases Canada supplied a large portion of the total world requirements;¹⁵ therefore, she would feel the full impact of any external disturbances. The weak condition of the international market for the two most important commodities, wheat and newsprint, rendered the situation all the more precarious.

The growth of the specialized exporting industries was associated with very heavy expendi-

tures on fixed equipment. The economy became geared to a high rate of capital investment; if anything curtailed this investment, a serious problem of unemployment would arise. Furthermore, these investments in capital facilities were financed in a way which greatly increased the overheads and rigidities. The large fixed interest costs of private industry and governments would make adjustments to falling export incomes extremely difficult. Added to these rigidities were those which arise out of increasing urbanization, industrial concentration and centralized financial control.

The rapidly increasing per capita real income during the twenties both in Canada and in other countries was another source of instability. The more income rises above the requirements of bare subsistence, the more unstable the economic system tends to become. The expenditures on personal services, comforts and luxuries may be sharply reduced or postponed when confidence is shaken by economic disturbances. The higher the proportion of income devoted to non-essentials and the more specialized the productive resources, the more severe and far-reaching is the contraction which results from the curtailment of such expenditures. In 1929 the average per capita real income in Canada was one-third higher than in 1920. In the latter year large sums were spent on automobiles, radios, household appliances, new houses, and on other semi-luxuries or postponable items. A sharp reduction in these outlays would create difficult problems of unemployment and readjustment.

At the end of this decade Canada had attained a high level of prosperity, but the increased specialization, the great dependence upon raw material exports, large overheads, stubborn rigidities, and a relatively high per capita income greatly enhanced her vulnerability to economic fluctuations. These fluctuations might arise from external developments, or from geographical and climatic factors in Canada, or as a result of errors of policy in the past and the limitations inherent in the Canadian economic and political structure, but all had the common characteristic of being, at the time, uncontrollable by any means then at the command of Canadian governments.

2. PUBLIC FINANCE

The circumstances of the twenties included no spectacular changes such as those which brought the steep increases in government liabilities and expenditures associated with the wheat boom, the War and the immediate post-War conditions. Between 1920 and 1930 the total per capita debts and expenditures of all governments rose but 13 per

¹⁵ In 1930 Canada supplied 32 per cent of the world's exports of wheat, 63 per cent of the world's exports of newsprint, 14 per cent of the world's exports of copper, 12 per cent of the world's exports of lead and zinc, and 31 per cent of the world's exports of aluminium.

cent and 9 per cent respectively. During this period, however, there were significant changes in government responsibilities and in the problems of Canadian public finance. Public welfare and highways occasioned the most rapidly increasing costs of government and these fell almost entirely on the provinces and the municipalities. Thus, while the total per capita debts and expenditures of the Dominion declined, those of the municipalities rose by over 20 per cent and those of the provinces by over 70 per cent. The provinces, which were required to finance and administer the major portion of the expanding public functions, acquired a greatly enhanced importance in the governmental structure of the country.

Cautious Policy of the Dominion—consolidation of past developmental projects and avoidance of responsibility for expanding services

Throughout the period, the Dominion resisted the temptation to embark on new services and until the later years of the decade it enforced a rigid economy on all controllable expenditures. By 1926 a substantial reduction in current outlay had been effected. However, in the boom prevailing after 1926, expenditures rose slowly through diffused expansion of existing services. The only significant new obligation assumed was the assistance to provincial old age pension schemes. The cost of general government rose substantially and there were moderate additions to the expenditures on agriculture and national defence. Offsetting these, the position in 1930 showed a substantial decline

in current payments on transportation, due mainly to the reduced deficits of the national railways. Although the outstanding debt of the Dominion rose by \$250 million, owing to the expenditures necessary to round out the national railway properties and for the extension of branches in the Prairie Provinces, the total interest charges decreased, partly because of refunding at lower rates of interest and partly because of the improved earning position of the Canadian National Railways.

In its endeavour to ease the burden of taxation, the Dominion at least managed to simplify the tax structure by reduction and elimination of special War taxes. Rising imports and rising prosperity boosted customs and excise receipts thus making it possible to cut the special levies. The business profits tax and some minor taxes were entirely abandoned. By successive cuts the sales tax was whittled down from 6 to 1 per cent. The corporation income tax was lowered. The income tax on persons was cut and the exemptions repeatedly raised. In this way the indirect taxes of customs and excise resumed some of their former importance in the federal revenue system. In 1913 virtually all Dominion revenues came from these two sources. In 1921, with the yield of special taxes at its peak, customs and excise produced little more than one-third of total revenues. In 1930 they produced a sum approaching two-thirds of total revenues. In its whole fiscal policy the Dominion was labouring for a return to pre-War "normalcy"—although it was no longer dealing with the pre-War economy.

TABLE 39.—GOVERNMENT EXPENDITURES, CURRENT ACCOUNT, 1921 AND 1930

(Thousands of Dollars)

	Municipal		Provincial		Dominion		Total ^(a)	
	1921	1930	1921	1930	1921	1930	1921	1930
Net Debt Charges.....	36,944	55,740	14,384	29,476	152,488	149,098	202,475	232,522
Defence.....	—	—	—	—	17,249	23,256	17,249	23,256
Pensions and Aftercare.....	—	—	—	—	53,688	55,341	53,688	55,341
Public Welfare.....	18,786	31,510	12,437	34,678	4,911	17,696	36,134	83,882
Education.....	66,280	84,705	20,850	33,775	924	702	88,057	119,191
Agriculture and Public Domain.....	—	—	9,174	21,241	17,596	23,296	26,722	44,484
Transportation.....	30,962	42,159	8,119	28,328	41,666	29,063	80,747	99,570
Subsidies to Provinces.....	—	—	—	—	12,212	19,036	—	—
General Expenditures— Justice, Legislation, General Government and Miscellaneous.....	51,911	71,614	25,689	35,902	^(b) 53,733	^(b) 70,332	^(c) 131,333	^(c) 177,849
TOTAL.....	204,883	285,728	90,653	183,400	354,467	387,844	636,405	836,095

^(a) Inter-governmental payments eliminated.

^(b) Includes Post Office deficit of 4,045.

^(c) Includes Post Office deficit of 4,021.

Rapid Expansion of Provincial-Municipal Expenditures—provinces assume major share of cost of expanding services; public welfare and highways

Of the \$200 million increase in current expenditures at all levels of government between 1921 and 1930, the Dominion accounted for only \$33 million. Of the \$1½ billion increase in total outstanding debt of all governments in this period, only one-quarter billion dollars was incurred by the Dominion (including the Canadian National Railways). The reluctance of the Dominion to embark on new services or to give assistance in financing them meant that the weight of the new demands fell on the provinces and municipalities. Moreover, the demands which loomed up in the twenties were for services falling primarily, if not solely, within the constitutional powers of the latter governments. Thus there was a marked rise in both provincial and municipal debt and current expenditures. The \$1 billion addition to the debt of the provinces and municipalities was largely incurred for public utilities, highways and various projects of development. The greater part of the \$173 million increase in the current expenditures of provincial and municipal governments in this period was due to increased debt charges arising out of these capital investments and to increased current expenditures on public welfare and highways. The provincial and local governments had either special interests or special responsibilities in these fields.

With the virtual disappearance of the agricultural frontier, the increasing specialization of occupations, and the continued drift from the country to the city which accompanied greater industrialization, the self-sufficiency of individuals, families and communities continued to decline. The risk of individual misfortune which had formerly been carried by the individual himself, the family, or by informal community assistance and charity, was throughout this period assumed to an increasing extent by governments. At the beginning and again at the end of this decade the provinces and the Dominion, as well as the municipalities, made payments for the relief of unemployment. Through the initiative of the Dominion a provincially-administered old age pensions scheme was launched during the twenties, which involved the provinces entering the scheme in the responsibility of providing half the rapidly mounting cost. The provision of mothers' allowances was extended. A growing realization of the vital public interest in public

health led to the extension of free curative and preventive services and to enlarged support of hospitals and similar institutions.

Despite the economic and social changes which manifested themselves in a pronounced manner in the twenties, Canadians adhered to the belief (quite appropriate in a simpler society) that the municipalities were the proper agencies to bear any necessary public responsibility for social welfare. Provincial governments through their assistance to welfare activities made many amendments to this doctrine. But the Dominion was barred from accepting any responsibility except, as it proved, when a public welfare problem overwhelmed both the municipalities and the province. Thus the greater part of the growing burden of these services fell upon the latter governments.

Between 1921 and 1930 current public welfare expenditures of all governments rose 130 per cent. The Dominion share of this increase was confined almost entirely to the financial support given to provincial old age pensions schemes and relief grants which reappeared again in 1930. Three-fourths of the added outlays were borne by the provinces and municipalities. However, at the end of this period public welfare still absorbed less than one-fifth of the provincial-municipal revenues. Buoyant economic conditions throughout the greater part of the twenties kept public welfare needs at a minimum and masked the fundamental social and economic changes which had taken place. There was no obvious indication of the potential magnitude of the financial responsibilities which the provinces and municipalities had assumed.

Traditionally, roads and highways were a provincial and local responsibility in Canada. In a smaller, more compact and more evenly settled country, the coming of the motor vehicle would have precipitated a national highway program. Because great distances and natural obstacles divided the areas of settlement in Canada, the motor vehicle was at first used only for inter-urban and short-haul purposes. The demand for national highways was long in emerging and the Dominion, struggling with its railway problem, limited its contribution to highway development in this period to temporary grants-in-aid to the provinces between 1919 and 1928. The reconstruction of local roads into a network of highways capable of carrying the ever-growing motor traffic fell to the lot of the provinces and the municipalities. The automobile promoted the growth of suburban areas around the larger cities, thus extending the areas which required

new community equipment and various municipal services. The rapid increase in the use of the automobile throughout the twenties made suburban development, as well as highway construction and maintenance, an ever heavier burden.

Current outlay on highways by all Canadian provinces and municipalities was nearly doubled between 1921 and 1930. Capital investments in streets, highways, bridges, and ferries rose from \$364 million to \$743 million. Owing to the enforced restrictions on capital expenditures during the War, relatively little progress was made with highway construction until the twenties. In most provinces ambitious programs were launched early in the period. But the increasing speed, weight and number of vehicles rapidly pushed even new roads into obsolescence. Main highways were soon costing as much as railway lines of high standard. The demand throughout the period was much higher than the capacity of most provinces and municipalities to provide them.

The British North America Act secured the provinces in control of education. During this period a number of factors contrived to increase the cost of this function. An equalitarian philosophy demanded the widest possible extension and constant improvement of educational opportunities. The growing complexity of the economy required an increasing variety of skills which could only be supplied by a more specialized and more expensive educational system. Moreover, the predominance of younger people among the immigrants who flowed into the country after 1900 altered the normal age distribution of the population and brought a sharply increasing number of children to the schools in the twenties. The possibility of relieving the consequent growing burden on the provinces and municipalities through substantial federal aid to education was limited if not entirely excluded by latent racial and religious issues. The Dominion made special temporary grants-in-aid for agricultural instruction and technical education which were of some assistance in this period, but these were not renewed when they expired. In the result virtually the entire burden of mounting educational costs remained with the provinces and the municipalities.

During this period the provinces were more than ever concerned with promoting the development of their natural resources. Added attention was given to the protection of valuable forest reserves against fire and insects. Conservation of fish and game was linked with active promotion of the tourist trade. Roads were built and geological surveys undertaken to encourage mining development. Various

expenditures were made to encourage immigration and settlement in new areas. Consequently, between 1921 and 1930, the current outlay on public domain and agriculture rose from \$9 million to \$21 million.

The public utility projects pushed forward by the provinces during this period were closely allied to their interests in public domain and development. Ontario invested heavily in hydro and Saskatchewan, Manitoba, New Brunswick, and Nova Scotia made capital outlays on provincial electric-power systems. The Prairie Provinces extended and improved their telephone facilities. The total provincial capital investment in public utilities (excluding railways) rose from \$172 million in 1921 to \$330 million in 1930. These investments, however, were almost entirely self-supporting and while they added substantially to total governmental debt, they did not add (with the exception of telephones in Alberta) materially to the burden of debt charges.

The Doubling of Provincial Revenues—appearance of new sources; liquor control, gasoline taxes and motor vehicle licences.

While the Dominion pursued a negative policy, avoiding new obligations and striving to cut down existing ones, the provinces and municipalities, taken as a whole, extended some of their old activities in a marked fashion and assumed new responsibilities of an undefined scope. Greatly increased revenues were necessary to meet some \$173 million increase in annual expenditures of 1930 over 1921. Municipalities provided for their added costs by increased returns from existing sources of revenue, while the provinces relied partly on the increased yield of old sources and partly on new sources which they discovered.

The tax on real property remained the mainstay of municipal revenue. In 1930, as in 1921, it provided over 80 per cent of the municipal receipts. The post-War slump which drove down property values caused many municipalities acute embarrassment in the early years of the decade. Moreover, the increased use of the automobile had a serious and adverse effect upon the tax base in many of the larger urban centres. At the very time when it was compelling large expenditures on the improvement of streets, it promoted the rapid growth of new residential districts outside the boundaries of the city. This flight to suburban areas had a depressing effect upon property values within the central municipality. However, the economic expansion of the twenties, combined with

TABLE 40.—GOVERNMENT REVENUES, CURRENT ACCOUNT, 1921 AND 1930
(Thousands of Dollars)

	Municipal		Provincial		Dominion		Total ^(a)	
	1921	1930	1921	1930	1921	1930	1921	1930
Federal Subsidies.....	—	—	11,865	14,276	—	—	—	—
Taxes—								
Customs Import Duties.....	—	—	—	—	105,887	131,209	105,887	131,209
Excise Duties.....	—	—	—	—	36,755	57,747	36,755	57,747
Manufacturers' Taxes.....	—	—	—	—	6,639	10,474	6,639	10,474
Sales Taxes.....	—	—	—	—	61,273	20,147	61,273	20,147
Corporation Taxes.....	—	—	11,162	18,520	84,008	45,961	75,170	64,481
Succession Duties.....	—	—	9,724	20,780	—	—	9,724	20,780
Income Taxes on Persons.....	73	3,896	485	2,122	39,821	26,624	40,379	32,642
Gasoline Taxes.....	—	—	—	23,487	—	—	—	23,487
Real Property Taxes.....	189,656	257,118	9,720	6,708	—	—	199,376	263,826
Amusement Taxes.....	—	—	3,032	4,525	—	—	3,032	4,525
Other Taxes.....	17,956	21,760	1,199	1,534	6,140	4,531	25,295	27,825
Sub-Total—Taxes.....	207,685	282,774	35,322	77,676	320,323	296,693	563,330	657,143
Motor Vehicles, Automobile Licences, etc....	—	o	8,381	19,907	—	—	8,381	19,907
All Other Licences, Permits and Fees, Fines and Penalties.....	8,010	11,294	8,360	10,024	2,860	3,703	19,230	25,021
Public Domain.....	—	—	14,786	17,037	3,542	2,297	18,328	19,334
Liquor Control.....	—	—	7,856	30,985	—	—	7,856	30,985
Sale of Commodities and Services.....	1,165	3,171	747	1,159	2,358	2,745	4,260	7,075
Other.....	13,537	19,916	3,083	2,759	3,425	8,605	18,679	29,457
TOTAL.....	230,387	317,155	90,400	173,823	332,508	314,043	640,064	788,922

^(a) Inter-governmental receipts eliminated.

^(o) Particulars not available; included with All Other Licences, Permits and Fees.

rapid urban growth, came as an important counter-acting influence, supporting property values and strengthening the tax base for the time being. While all other sources of municipal revenue yielded \$20 million more in 1930 than in 1921, the tax on real property yielded an additional \$67 million. Anything which had an adverse effect on real estate values would undermine Canadian municipal finance.

The capacity of the provinces to discharge the responsibilities they had assumed in the fields of public welfare, education, highways and public domain rested very largely on the remarkable increase in revenues derived from liquor control, motor vehicle licences and gasoline taxes. Total provincial revenues in 1930 were nearly double those of 1921; more than two-thirds of this increase was derived from the additional yield of these three items. Provincial revenues from motor vehicle licences and liquor control rose by \$11 million and \$23 million respectively during the period. Most important, the provincial gasoline taxes, which had not yet been imposed in 1921, were yielding more than \$23 million in 1930. Total

provincial revenues from corporation taxes, and succession duties doubled during the period but the total increase derived from these sources was considerably less than the increase provided by the profits of liquor control alone. The provinces, which had once been expected to rely almost entirely on revenues from public domain and the unconditional federal subsidies, drew only 10 and 8 per cent respectively of their revenues from these sources in 1930.

The Vulnerability of the Provincial Fiscal Systems—the reluctance of the Dominion to relieve or assist the provinces and to compensate for the great regional disparities

During the twenties the provinces, relying on new-found sources of revenue, increased their expenditures very considerably. Much of their current outlay was on fixed charges and, therefore, uncontrollable. The responsibility for public welfare was laden with contingent commitments, and their weight would vary inversely with the ability to carry them. During a depression their

total expenditures were certain to rise. Their revenues were, to a considerable extent, drawn from semi-luxury "consumption taxes" which were equally certain to give a decreased yield when there was a contraction in incomes. The economy would reveal, under the stress of economic reverses, great disparities in the width and adequacy of the different revenue bases and in the vulnerability of fiscal systems. The combination of falling revenues and rising costs would affect the different regions very unequally. The inherent weaknesses in the position of the Maritimes were clearly exposed early in the decade. The whole structure of provincial and municipal government on the Prairies was highly vulnerable, and almost entirely dependent on the maintenance of the favourable export position of a single commodity: wheat. British Columbia too was heavily dependent upon favourable prices for its exports. Relatively speaking, the Central Provinces, with a more diversified economy and with their access to the national pools of wealth, had much the most secure and advantageous position.¹⁶ In times of prosperity these disparities, even though disturbing, were still tolerable. In any period of sharp distress some kind of equalizing action by the Federal Government would be inevitable.

During the twenties the Dominion Government took the lead in launching a system of old age pensions and agreed to match provincial appropriations for that purpose under certain specified conditions. At the beginning and again at the end of the period the Dominion made emergency grants to the provinces to assist in the relief of unemployment. When the serious plight of the Maritimes became an unmistakable fact, the Dominion took steps to assist them and increased subsidies, in accordance with the findings of the Duncan Commission, sufficiently to cover the current deficits. This was an admission that when a province had demonstrated in a painful way that it was unable to fulfil its responsibilities, the Dominion was prepared to extricate it from its immediate difficulties. Only in extreme cases was the Federal Government willing to undertake equalizing action. In all other circumstances the Dominion shied away from new financial burdens and studiously resisted suggestions that it should aid the provinces to carry their mounting obligations.

There were a number of reasons for this attitude on the part of the Federal Government. Its own burden of debt and the costs of reorganizing the government railways were acutely inhibiting influences. Intent upon retrenchment and reduction of debt charges, it insisted that the British North America Act laid the responsibility for meeting the new demands at the doorsteps of the provinces and the municipalities. For the same reason it was little disposed to assist the provinces by making conditional grants-in-aid for specific provincial services. Moreover, the conditional grant was far from being generally approved as an appropriate device in the hands of the Federal Government.

Conditional grants were first used in 1913 when federal assistance to the provinces for agricultural instruction was granted for a ten-year period. As part of the reconstruction program at the close of the War, similar grants were provided for assistance to highways, technical education, control of venereal disease, and maintenance of employment offices. These grants were either experimental or were given under extraordinary circumstances. Most of them were given for but a limited period of time. However, there was a body of opinion which favoured vigorous federal initiative and leadership for national purposes, even in fields where the primary responsibility rested with the provinces. It supported the further extension of the technique of the conditional grant as an instrument of national policy. The opponents to the use of such grants objected on the ground of the well-known argument that a government which spends public funds should bear the full responsibility of levying the taxes necessary to provide the money. They also emphasized that a harmonious federalism depended on the Dominion respecting the untrammelled independence of the provinces in their own sphere. They argued that attempts to ensure careful spending of federal funds would involve the Dominion in a dangerous interference with the autonomy of the provinces. This latter view was dominant in federal politics throughout the greater part of the twenties. Thus theory supported practical considerations of economy in rejecting conditional grants. The system of conditional grants was not extended and the subventions for agricultural instruction, highways, and technical education were allowed to lapse. Apart from exceptions already noted, the Dominion was bent on avoiding new obligations in the post-War period. The general prosperity of the later years of the twenties made this possible without any

¹⁶ Ontario and Quebec in 1930, with 60 per cent of the total population of the Dominion, were collecting 57 per cent of the total succession duties. These Provinces had large reserves of revenue in their ability to make levies on national business organizations whose principal offices and property were located within their borders.

immediate repercussions in the provinces, but it did not prevent the provinces getting into seriously exposed positions.

Signs of approaching difficulties were not wanting. The distress of the Maritimes was met temporarily by the award of the Duncan Commission which nearly doubled their subsidies. At the Dominion-Provincial Conference of 1927, when the award was approved by the other provinces, all the provinces except Ontario and Quebec gave notice of further claims. They complained that their fiscal resources were not adequate to their obligations, and proposals ranged from the assumption of new services by the Dominion to the withdrawal of the Dominion from certain fields of taxation. The reply made by the Dominion Minister of Finance to these various claims and suggestions mirrors faithfully the attitude of the Dominion throughout the twenties. If the obligations of the provinces were heavy, so were those of the Dominion. The Dominion was anxiously concerned over its heavy debt and the importance of maintaining Canada's credit so as to encourage the flow of investment into the country. The Dominion could neither undertake large new responsibilities nor relinquish fields of taxation. The suppliant provincial premiers had to derive what solace they could from the reminder that Dominion policy in lowering taxation helped to clear the field for heavier provincial taxation.

Despite the anxiety of the Dominion to reduce its obligations the total annual sum transferred by way of subsidies and conditional grants to the provinces was higher in 1930 than in 1921. The award of the Duncan Commission, along with the payments on account of old age pensions, more than cancelled the savings secured through the lapse of several conditional grants. In 1930 a federal grant of \$3 million for relief made its appearance. Dominion payments to the provinces which had stood at \$18 million in 1921, amounted to almost \$24 million in 1930. However, their relative importance declined. Dominion subsidies and grants which had covered 20 per cent of the expenditures of provincial governments at the opening of the period covered only 13 per cent of those expenditures at its close. In their assumption of new responsibilities, the provinces had to rely almost entirely on their own resources. Depression was soon to show the common vulnerability of their fiscal systems and the great disparities in the abilities of the different provincial governments to carry their increased burdens.

3. DOMINION-PROVINCIAL RELATIONS

Eclipse of Federal leadership—completion of developmental program, reluctance to assume new financial burdens, and lack of new national objectives

The post-War period marked the end of an era in Canadian federalism. Up until the War, Dominion Governments had pursued, subject to minor hesitations and variations, a number of national policies which brought about an economic integration of the country and helped to make political unity a fact instead of merely an aspiration. The War and the problems of demobilization served to continue into the twenties the federal leadership to which the country had become accustomed. But after the liquidation of the War policies a new situation presented itself. The policies of all-Canadian transportation and western settlement had been brought to fruition. The tariff, though revised downwards to some extent, was a bone of regional contention rather than a unifying influence. During the period the consummation of Dominion status and the securing of a measure of international recognition brought the principal external policies of the country to a successful conclusion. The Dominion had completed the concrete, positive tasks which the Fathers had set it to do and no broad new national objectives emerged to unite people behind federal leadership. Indeed, the discussions over national policies were much more concerned with assessing their past effects than with charting a national course in the post-War world.

The social and political chaos loosed in the world by the War was manifested in Canada by the disorganization of the federal political system. During the first half century of Confederation, Canadian politics had been distinguished by the solidity of party loyalties and by the duration and stability of party administrations. But the Liberal Party was disorganized by the conception issue and the Union Government disintegrated rapidly after the conclusion of the War. Federal politics in the first five years of the period showed the stultifying effect of this change. In the election of 1921 the Liberals got a nominal majority of only a few votes over all parties. The 65 Progressives, representing a revolt against the old national policies, held the balance of power in the House of Commons. From 1921 to 1926 the composition of the House of Commons in which there were three parliamentary groups, none of them constituting a

definite and stable majority of the House, discouraged the forming and carrying through of consistent and vigorous government policies.

There were other reasons why the Dominion did not embark on vigorous action. The public demand for increased government services in the twenties mainly concerned things which were, in the first instance, at least, the constitutional responsibilities of the provinces. A compulsory national wheat board was beyond the peace-time powers of the Dominion. While the Government seemed generally sympathetic to a national scheme of unemployment insurance, it was unable to embark on it without the co-operation of the provinces.* Moreover, the heavy debt charges of the Dominion which, by 1921, were one-and-a-half times the total Dominion current expenditures of 1913, were a matter of anxious concern to the Government and tempered any regret it may have felt that the initiative in most current problems rested with the provinces.

The only important thing the Dominion did in this decade to overcome the constitutional obstacles to federal action was to encourage the establishment of provincially-administered old age pensions schemes with offers of financial assistance. This assistance recognized a social problem which was reaching serious proportions. The wave of immigrants which reached the country in the early years of the century was bound to produce at a later date a wave of persons reaching the end of their active working lives. Those of mature age who had come to Canada in the early days of the wheat boom were ending the working period of their lives in increasing numbers in the late twenties. A greater proportion of these than of the younger immigrants or of the native born were unable to lay by a provision for their old age. They swelled seriously the ranks of the aged poor at a time when changes in the economic and social structure were intensifying generally the problem of old-age dependence. The heavy war casualties also contributed to the sudden emergence of the problem since many aging parents had lost the source to which they would normally have looked for support. The burden of the care of the aged poor over-taxed the resources which had supported them in the past and, with other problems of public welfare making increasing demands, the provinces were reluctant to assume such a heavy charge alone. The Federal Government modified its principles and came to their assistance.

With this important exception, the Federal Government did not wrestle with the social problems of the new age. Indeed, during the rising prosperity of the twenties few were aware of their existence. "Normalcy", pursuit of wealth, confidence in high wages as the road to social security, definite expectation that "normalcy" meant a very rapid advance in material prosperity and that the full utilization of new techniques would not be retarded by economic conditions such as mass unemployment, represented in Canada, as in many other countries, the prevailing temper of the time. Given these beliefs there seemed less need for federal controls. There was no broad public support for a vigorous policy of the Dominion in the field of social welfare. In domestic affairs it contented itself with detailed modifications and amplifications of old-established national policies.

Ascendancy of Provincial Governments—development of provincial resources, aggressive highway programs and extension of welfare services greatly enhance their importance and strengthen their political support

The provinces were not affected by war weariness and there were many things to be done in the provincial sphere which solid majorities would support. The War had put a damper on provincial expenditures and many needs had accumulated. Each province proceeded to meet them in so far as its resources permitted. The national developmental policies, expressed in railways and canals, were at a standstill, while new provincial programs of development, expressed in highways and water-power, were in the ascendant.

An immediate result of this extended range of activity was to add to the prestige and power of the provincial governments. The provinces owned the natural resources which had become immensely valuable through the development of new techniques. A tribute to their new importance was the determination which the Prairie Provinces displayed in this period to get control of their natural resources.* Labour and capital began to depend on provincial highway and other developmental programs for jobs, contracts, and various industrial opportunities as they had formerly been dependent on railway construction and the schemes of development initiated by the Federal Government. The "new men" of the period, the adventurous figures who discovered and developed the wealth of the Pre-Cambrian Shield, exhibiting all the vigour and self-confidence of a rising class,

* *Debates House of Commons, 1921, Vol. II, pp. 1073-4.*

associated themselves, as a rule not with federal politics but with those of the provinces where the key to their interests and aspirations lay.

Moreover, provincial governments assumed a larger importance in the daily lives of the people. At the Dominion-Provincial Conference of 1927 Premier Taschereau pointed out that "the provinces were more in contact with the people, educating them, building their roads, and looking after their health." From the point of view of the recipients, they became also the donors of old age pensions; they provided mothers' allowances and minimum wage legislation. The popular basis of provincial political power was being solidly laid at a time when the Dominion was losing its intimate touch with the people, and when its developmental projects no longer gripped the imagination and no longer gave increasing employment to labour and capital. Instead the Dominion was intensively engaged in making vexatious levies for the payment of old debts.

The combined effect of these factors was to elevate the provinces to a new position in Dominion-provincial relations. The control over the public domain, the jurisdiction over public welfare, and over those economic matters in which the courts had sustained them, took on new content and significance. The provinces, which had once been compelled to struggle to escape complete domination by the Dominion, had come into a goodly heritage of their own.

Federal Concessions to Provincial Claims—Maritime claims, natural resources question, water-power, Dominion-Provincial Conference, 1927

The common interest in western development had, for twenty-five years, continuously strengthened East-West bonds of unity. In the twenties a variety of regional interests began to compete seriously with this common interest. British Columbia and the Central Provinces acquired important direct contacts with external markets which lessened their dependence on internal markets. The political revolt in the immediate post-War years of western agriculture against the old line political parties has already been noted. The continuance of the post-War depression in the Maritimes up until 1925-26 seemed to argue that the national economic integration was of little advantage to the Maritimes and they attacked rather than supported the operation of the national policies on which it was based.

The severe economic difficulties under which the Maritimes laboured in the early twenties aroused profound dissatisfaction, particularly after the contrast of marked recovery in the rest of Canada became apparent. By 1924 these adverse conditions produced a formidable movement for the vindication of "Maritime Rights", led and directed by the business interests of the region. Economic conferences called at Moncton and Charlottetown in 1925 studied a wide range of economic problems and gave extended publicity to their final resolutions. While the formulated demands called for a solution through federal action, there were some who advocated secession from the Dominion as the only escape from an intolerable situation.

The economic and financial distress of the region, combined with the vigour of the agitation, led in 1926 to the appointment of the Duncan Commission to investigate Maritime claims. The Province of Nova Scotia filed a comprehensive brief, dealing in detail with the whole range and history of Dominion-provincial relations as they affected the Maritimes. New Brunswick and Prince Edward Island accepted it as the basis of their case. All this material was marshalled together in a single volume for the purpose of proving that the Maritimes had never obtained the substance of the benefits promised them at the time of Confederation and that consequently they had never enjoyed a welfare and prosperity comparable to those of other parts of Canada. The brief maintained that the Maritimes had never received their promised share of the internal commerce which the union was designed to promote and that this failure flowed from the fact that the national transportation and tariff policies of the Dominion had been framed and enforced in callous disregard of the rights of the Maritimes.

It is not the present purpose to consider the justice of these claims nor to discuss the measures of amelioration which the Commission proposed. It is rather to draw attention to the political significance of the agitation. An entire region of the Dominion, moved apparently by a common sense of injustice, protested against the inequitable operation of the national policies. Whatever rights may have been involved, the plight of the Maritimes was serious. A region, suffering from these difficulties and animated by a sense of injustice, found that its most immediate interest in national affairs was to secure some recognition of its regional troubles.

By the time the Commission on Maritime claims had reported the long-continued agitation of the Prairie Provinces for control of their natural resources had become very insistent. It is significant that at the Dominion-Provincial Conference of 1927 where both questions were considered, the Maritime Provinces and the Western Provinces supported each other's claims. The older provinces had retained the ownership of the natural resources within their boundaries but the Dominion, under the Manitoba Act, had reserved the western lands "for the purposes of the Dominion". Dominion control of these lands had been the foundation of the national policy of western settlement and as well of the policy of a transcontinental railway. As settlement was now well advanced, it was plausible to argue that the purpose of the Dominion had been achieved, and that the lands might now be transferred to the provinces. However, the Prairie Provinces were not content merely to secure control of the public lands. In this period of regional demands on the Federal Government, they insisted that the retention of the western natural resources had always been a violation of certain inherent "provincial rights" which antedated and were in no way abrogated by Confederation. Accordingly, they claimed that the provinces were entitled to ask the Dominion to account for all the material advantage it had derived from the lands after 1870. They, therefore, sought an accounting from the Dominion on this basis.

The Dominion Government conceded the substance of these claims in 1928, when after a conference with representatives of the Government of Manitoba it agreed that Manitoba should be "placed in a position of equality with the other provinces of Confederation with respect to the administration and control of its natural resources, as from its entrance into Confederation in 1870". The Turgeon Commission was appointed to "inquire and report as to what financial readjustments should be made to this end". The Commission interpreted this as an instruction to estimate whether "Manitoba is in as good a financial position as she would probably have been in had her right to the administration and control of her natural resources been conceded from the beginning". The inquiry was directed toward reaching some kind of an estimate as to whether the alienation of Manitoba lands "for the purposes of the Dominion" as set out in the Manitoba Act had caused loss to the Province. Alienation of lands for public purposes within the Province was regarded by the Commission as affording but a slight basis for claims for compensation.

"We are placing", said the Commission in its report, "a light appraisal on the loss to the Provincial Government in respect to homestead land." There was, it was held, no basis for a claim of compensation for land given to aid the construction of branch lines within the Province. For lands allotted to the Canadian Pacific Railway for the construction of its main line outside the Province, compensation was held to be due. The Commission, by an intricate and ingenious calculation, estimated the cost of these alienations to the Province and made an award. A similar procedure was followed with respect to the claims of Saskatchewan and Alberta;¹⁷ and Commissions, headed by Mr. Justice A. K. Dysart, made awards to these Provinces upon the precedent set by the Turgeon Commission in the case of Manitoba. The transfer of the natural resources to the Prairie Provinces had important symbolic significance. It marked the completion of the great effort of the Dominion to achieve nation-wide expansion through national direction of western settlement. The success of the Western Provinces in getting the Dominion to account for its stewardship as well as the recognition of the claims of the Maritimes announced a new era in Dominion-provincial relations, an era in which regional disparities, regional difficulties, and regional ambitions became a principal concern of federal politics.

Another Dominion-provincial issue of importance in the latter years of the decade was that of the development of the St. Lawrence Seaway Canal. Proposals for development for navigation and power purposes were under consideration as early as 1920. Quebec, however, opposed the development of navigation lest it prejudice the port of Montreal, while both Ontario and Quebec opposed development of power by the Dominion, claiming that water power within the province, even in navigable waters, was a matter of provincial ownership and jurisdiction. Requests were made at the Dominion-Provincial Conference of 1927 for reference of the question of jurisdiction to the Supreme Court of Canada, and the following year the Dominion referred ten stated questions to the Court, but owing to the generality of the

¹⁷ The Dominion Government's proposal was that there should be, with respect to Saskatchewan and Alberta, an inquiry "in order that the provinces might be placed in a position of equality with the other provinces as from September 1, 1905", the day upon which the provinces came into being. The Saskatchewan government contended that the adjustment should go back to 1870, the date of the transfer of Rupert's Land to Canada. A stated case was submitted to the Courts and in 1931 the Supreme Court held that the province had no claim to the natural resources of the area prior to September 1st, 1905. In the following year this judgment was upheld by the Judicial Committee of the Privy Council.

questions the answers were far from conclusive. In the meantime the Quebec Legislature had granted a private corporation a charter for a power canal on the Soulanges section of the proposed seaway development. Although the company subsequently had to apply to the Dominion for permission to divert water from Lake St. Francis, the undertaking was begun and, after the opinion of the Court was delivered, permission for the diversion was given by the Dominion. The discussion in Parliament on the permit indicated that, despite the inconclusiveness of the opinion of the Supreme Court on the matter of jurisdiction, the Dominion had substantially conceded the provincial claims to ownership and control of water power in navigable waters.

During the twenties the method of amending the Constitution for the first time became an issue between the Dominion and the provinces. The method of amending a federal constitution is always difficult to work out, but the problem had been finessed in 1867 by omitting from the British North America Act all reference to amendment and thus leaving amendment to the enacting authority—the Imperial Parliament. The change of status of the Dominion during and after the Great War gave rise to a widespread demand in the twenties for the transfer of the power of amendment to Canada. This inevitably raised the question of method and at the very time that the prestige of the provinces was in the ascendancy. The British North America Act had been amended six times, but on one occasion only—that of 1907 which concerned provincial subsidies—had the provinces been consulted. At the Dominion-Provincial Conference of 1927 the Dominion Government raised the question and recommended that Canada should have power to amend her own constitution, that the provinces should in all cases be consulted, and that for the amendment of a number of specified matters deemed fundamental the consent of all provinces should be required, but that in other matters the consent of the majority would be sufficient. Despite the consideration given to provincial sentiment, the proposal failed to carry, because of disagreement as to method and because certain provinces were opposed to any change in procedure.

A significant contribution was later made to the literature of constitutional theory (and hence to the controversy over methods of amendment) by the Government of Ontario when the Statute of Westminster, which was to formalize certain of the findings of the Imperial Conferences of 1926 and 1929, was under discussion. Ontario opposed

adoption of the Statute by the Dominion without consultation with and approval by the provinces on the ground that the Statute was in effect an amendment of the British North America Act, and that this Act was a compact between the provinces and as such could not be amended without their consent. Following the election of 1930 the new Government called a conference of the provinces and secured their approval of the Statute, thereby seeming to admit the validity of Ontario's argument.

No less significant than the apparent retreat of the Dominion on various constitutional matters were the growing demands for the expansion of provincial revenues at the expense of the Dominion. The Duncan Commission, as already noted, found that the Maritime Provinces were in a serious condition of fiscal need and recommended on one ground or another substantial increases in subsidies to these Provinces. The demands of the Prairie Provinces for the return of their natural resources were obviously aimed not only at establishing the constitutional equality of these provinces but at increasing their revenues as well. The Dominion-Provincial Conference of 1927 was the occasion for warnings from British Columbia of its difficult financial position, as well as for general demands, from virtually all provinces, for increased subsidies and for grants for such matters as highways and technical and agricultural education. The Conference also heard demands for enlarging the provincial tax base, British Columbia urging that the Dominion should withdraw from the income tax field, Manitoba that the provinces should be granted a fixed percentage of customs and excise taxes. All these incidents and demands were symptomatic of the narrow margin of safety in which the provinces were finding themselves, and indicated that any serious renewal of economic difficulties would increase their demands upon the Dominion.

Conclusions

Throughout this period the provinces were politically aggressive in undertaking new activities, in advancing their own affairs, and in securing concessions from the Dominion. In their difficulties, in their ambitions and opportunities, as well as in the disparities between them, several sets of common interests of a regional character emerged. These regional forces served to weaken the common interest in a national integration based on wheat. In the general prosperity of the twenties, which provided an expanding national income, the regional interests were harmonized amicably with-

out serious friction or serious sacrifice and the provinces were able, with more or less difficulty, to carry the new responsibilities they had assumed.

But the great depression which began at the end of the period, and which will be described in the next chapter, was to widen greatly the disparities, and to reveal both the insecurity of the foundation on which prosperity had been based, and differences

of interest which were extremely difficult to reconcile under conditions of sharply falling revenues. These differences of interest were to assume a new significance in an era of depression, when weaker provinces, overwhelmed in the struggle to carry new and old responsibilities, were to become financial wards of the Dominion, and the strongest provinces stood to gain by enlargement of provincial autonomy.

CHAPTER VI

THE DEPRESSION

1. WORLD DEPRESSION AND RECOVERY

*Economic Dislocations in the Post-War World—
Effects of the War, peace treaties and technological changes required basic readjustments in international economic relations*

The economic progress of the world during the twenties was impressive. Between 1920 and 1929 the per capita world production of primary commodities, and of manufactured goods rose 31 per cent and 38 per cent respectively. The quantum of world trade per capita increased by at least 30 per cent. It is remarkable that these striking advances in the world economy were possible while serious structural weaknesses continued to exist and were even intensified.

The war-stricken world of 1920 faced an economic order which was drastically changed from that which obtained prior to 1914. The demands of the conflict, the terms of the peace treaties and technological changes greatly altered the basis of international economic relations. There was a very substantial increase in the production of foodstuffs and raw materials in overseas countries. The manufacturing industries of the United States, the British Dominions and Japan received a strong impetus from the War-time decline in European exports. During the twenties machine methods of production spread throughout the world with increasing rapidity. Non-European countries were in the better position to benefit from important technological improvements and assumed the leadership in the production of automobiles, electrical appliances, radios, and the new textiles. New sources of power weakened the influence of coal as a dominant factor in the localization of industry. Northwestern Europe languished while one of its basic natural advantages was disappearing and areas with abundant supplies of water-power and petroleum came to the fore.

The shifts in manufacturing production were accompanied by equally important shifts in the production of cereal foodstuffs and industrial raw materials. The mechanization of agriculture greatly altered the competitive balance between the European peasant and the large-scale specialised farmer in overseas countries. The tractor, the combine, power-driven machinery, and the

motor truck were most effective on the semi-arid plains of America and Australia. Between 1914 and 1930 the number of acres of improved land per person engaged in agriculture on the Canadian Prairies rose by about 50 per cent. As a result of the War and lower costs in overseas countries, Europe's contribution to the total world (except Chinese) production of wheat fell from 56 per cent in 1909-13 to slightly over 40 per cent in 1926-29. During the same interval the European production of all cereals, sugar and potatoes decreased from 43 per cent to 39 per cent of the world total. The pre-War situation with respect to the geographical sources of industrial raw materials and the relative costs in the different areas was likewise greatly altered by technical improvements and new discoveries. In 1913 about 50 per cent (in value) of the world's non-ferrous metals were produced in America and Africa; by 1929 this proportion had risen to nearly 70 per cent. The share of new countries in the total physical output of petroleum, timber, newsprint, wood-pulp and vegetable oils showed similar increases. Furthermore the competitive relationship between old and new producers of bulky foodstuffs and raw materials was strongly affected by the abnormally depressed ocean freight rates of the twenties. In terms of the general price level, tramp steamer freights were fully 30 per cent below the pre-War rates. The opening of the Panama canal greatly shortened the distances of Pacific countries from Europe and the eastern shores of America. The substantial reductions in the costs of shipment brought many newly developing areas within the scope of the world market and increased the flow of heavy commodities to distant importers. These changes had wide-spread repercussions, but perhaps none was more significant than the increased pressure upon the peasant farmers of Europe.

The readjustments in international economic relations required by the rise of manufacturing in overseas countries, technological improvements and reduced costs of transportation were intensified by the post-War situation in international finance. The nature and the net balances of international indebtedness had greatly changed. A large proportion of the debts were for unproductive purposes. The financial world was entangled in a maze of

inter-governmental War debts and reparations. The United States emerged from the conflict as the world's second largest creditor, Germany as the largest debtor. The pre-eminent position of London as the regulator of the international gold standard by virtue of being the clearing centre of international transactions, the greatest lender on foreign account and the largest free import market, was immensely weakened. Its rivals, New York and Paris, played increasingly important parts, but neither had the experience or willingness to follow the long-range policies necessary for the maintenance of stable international monetary conditions out of which a rising volume of world trade could develop. International lending during the post-War period was sporadic; much of it was to governments which squandered the money on ill-advised and unproductive projects. The large proportion of short-term loans in international indebtedness added further to the instability of foreign investment. The restoration of the gold standard had brought with it the problem of undervalued (the United States dollar, the French franc and the Belgian belga) and overvalued (the British pound and the Italian lira) currencies. The strain resulting from the failure of national price levels to become adjusted to the re-established gold parities was temporarily relieved by the expedient of short-term borrowing. This factor, together with the general feeling of uncertainty and the development of the gold exchange standard, created a large volume of liquid funds which flowed nervously back and forth across the international exchanges. The solvency of important monetary centres came to be dependent upon a thin thread of confidence which temporary setbacks, political disturbances or rumours would quickly break.

Failure to Achieve Solutions to International Problems—resort to national controls and temporary makeshifts; development of agricultural crisis and over-extension of raw material production

The widespread economic dislocations and the unstable condition of international finance which were the outcome of war and of technical progress required substantial readjustments and a new integration of the economic world. They required extensive reallocations of resources, alterations of wage and price levels, a reduction of restrictions on trade and the sacrifice of vested interests. The magnitude of the changes involved was such that they could only be accomplished with international

co-operation to lower tariff barriers, maintain stable exchanges and make capital available. However, the efforts to achieve international co-operation failed dismally in the economic sphere as in the political. Nations sought the solution of these problems by the use of their own national controls and national policies. All the weapons in the arsenal of economic autarky were brought into play. Weak positions were protected, high cost producers were kept in production and obsolete equipment was preserved by rising tariffs, import quotas, cartels, government subsidies, "rationalization", restriction schemes, stabilization of prices, etc. A large part of the economic history of the first post-War decade chronicles superficial efforts to defy serious underlying dislocations. Europe struggled desperately to regain her pre-War position in an economic world which was greatly changed. This was particularly the case in agriculture. The peasant populations of Europe who in many instances formed the backbone of the state and whose political and social importance was great in all countries could not be sacrificed on the altar of cheap food. The consequences of the readjustment to the revolutionary increases in output and decreases in the costs of production in overseas countries were too drastic. This circumstance, together with the rising barriers against European exports of manufactures and the desire for self-sufficiency arising out of the fear of war, produced an extreme form of agricultural protectionism. The boundary revisions of the peace treaties intensified the harmful effects of this policy. Eight small states, each with its own currency and customs sovereignty, were carved out of three large empires. The economic system of Austria-Hungary, based on regions which "had grown up in mutual interdependence in the course of centuries", was broken into small parts and choked with tariff barriers. As European output expanded behind customs restrictions, and production in overseas countries continued to increase on the basis of natural advantages, a major crisis in world agriculture developed.

The unbalanced agricultural situation was accompanied by an increasing deterioration in the position of the raw materials. The old high-cost producers everywhere were threatened by new supplies and new processes. Obsolete or sub-marginal capacities were not withdrawn from production but were maintained in production by artificial means. For commodity after commodity, prices were artificially maintained or raised to bolster up uneconomic enterprises. None of the

various stabilization or restriction schemes had control over the total output and these attempts at increasing or fixing prices in the end served only to induce an abnormal expansion of production on the part of the non-restricted or non-conforming producers. Between the beginning of 1925 and the beginning of 1930, world stocks of twelve important raw materials rose by 40 per cent. During the same period world stocks of agricultural products increased by 50 per cent. These stocks hung menacingly over the markets ready to come down upon the price structure like avalanches.

The policies of creditor countries contributed much to the accumulating weaknesses in the structure of the world economy during the twenties. The attempt to collect increasing interest payments, to sell more and buy less, encounters an arithmetical impossibility. The unwillingness of the United States and France to lower, or even to stabilize, their tariffs so as to adjust their import balances in a manner consistent with their creditor positions produced an increasing disharmony between the flow of world trade and the requirements of international indebtedness. As the debts of borrowing countries rose it became continuously more difficult for them to export goods of sufficient value to meet the interest charges. They were forced to attract short-term funds by high interest rates and to lose their gold reserves with the result that their monetary systems were placed in an extremely weak condition. The strain was particularly great in Germany and in a number of agricultural countries especially those of south-eastern Europe.

The post-War world failed utterly to achieve a satisfactory compromise between the advantages of international specialization and national stability and security. For a time world economic activity and trade rose sharply because international lending and the constant renewal and increase of short-term balances filled the gaps in the balances of payments, because boom conditions were maintained by reconstruction in Europe and by the demand for investment and durable consumers' goods in the United States, and because heavy capital expenditures were being made for the exploitation of natural resources in new countries. However, by 1929 these temporary makeshifts and stimulants began to play out. The reconstruction boom in Europe was virtually completed. After the middle of 1928, international lending contracted rapidly. It became increasingly evident that productive capacities in a number of raw material industries were seriously over-extended.

Cereal prices were sagging and the agricultural crisis was imminent. At this conjuncture, a spectacular stock market boom in the United States sucked short-term funds to New York thus creating a world-wide stringency of credit. When this boom collapsed the catastrophe was at hand.

World Depression—cessation of international lending; strangulation of trade; breakdown of gold standards; sharp and disproportionate decline in raw material prices; severity of impact on debtor countries and exporters of primary products

In the United States confidence was severely shaken by the collapse of the stock market and the tremendous activity in capital investment was abruptly curtailed. The contraction of international lending, the attempt of creditors to recall their short-term funds and the general monetary tightness, put a heavy strain on the balances of payments of debtor countries. Germany was forced to cut down her imports sharply. Other debtors, who were mainly agricultural or producers of raw materials, were obliged suddenly to increase their exports. It was not long before many of the control schemes broke and loosed a flood of goods on the market. Russia reappeared as a big seller of raw products, chiefly wheat and timber. While the pressure upon the world market for agricultural goods and other raw materials was rising, Europe's ability to export manufactures to the United States and, therefore, to import foodstuffs and raw commodities was drastically curtailed by the Hawley-Smoot Tariff (1930). In order to protect their precarious financial and foreign exchange positions, or to shield the livelihood of their peasant populations, European countries imposed insurmountable duties and other restrictions upon the importations of foodstuffs. The impact of increased supplies upon mounting trade barriers and decreasing consumption resulting from the world-wide decline in investment produced an unprecedented fall in the prices of agricultural products and raw materials. In particular, the reduction of lending, weak and exposed monetary systems, and the general heightening of tariffs concentrated the full force of the depression upon those surpluses of goods which had to find an international market. Eventually, practically every country, creditor and debtor alike, had to, or chose to, make its adjustments not by an increase of trade, but by a reduction of imports.

Between 1929 and 1931 the value of world trade fell by 42 per cent. The drastic effects and uneven character of this decline are indicated by the 40 per cent drop in the export prices of seven leading overseas agricultural and raw material producing countries, compared with but a 15 per cent drop in the prices of their imports, which were mainly manufactured goods. The disparity revealed by this relation was one of the most characteristic and disruptive features of the world depression. The number and importance of the rigid elements in the economic system had greatly increased. The relative decline of equity investment in favour of bonds, and the extension of large-scale corporate enterprise added substantially to interest and other fixed costs. Wage rates acquired almost the rigidity of contractual interest charges. The elaborate economic overheads and frills that go with a rising standard of living proved to be particularly inflexible. The invariable costs were translated into administered or rigid prices most readily in the manufacturing and distributive industries where monopolistic conditions are most prevalent. The cartels were far more effective than their counterparts, the restriction or stabilization schemes for the raw materials. The producers of manufactured goods and the distributive trades, countered the declining demands by *restricting* output and maintaining prices; the primary industries, where small-scale individual enterprise is most general, tended to *increase* output against sharply falling prices. The former discharged their employees thus creating the problem of mass unemployment; the latter had to reduce drastically their standards of living and to default on many of their debts.

The divergence between the prices of raw materials and those of manufactured goods was a general phenomenon. It produced serious dislocations between the primary and secondary producers in nearly every country and placed a severe strain on the economic relations between raw material countries and those which exported finished goods. Between 1929 and 1931 the cost of the imports of the former rose approximately 30 per cent in terms of their exports; in two years the real burden of servicing their external debts increased by about 40 per cent. These abrupt changes quickly caused a number of breakdowns in the mechanism of international finance. Australia, New Zealand, and most of the Latin American countries were soon forced off the gold standard. The failure of the Austrian Kredit-Anstalt in the spring of 1931, which revealed the precarious situation in South-

eastern and Central Europe, started a succession of financial crises which sent the world headlong down the incline of depression. There was an immediate drive to liquidate the short-term foreign loans in Central Europe, especially Germany. The run on foreign funds brought on the failure of a number of important German banks, and the entire German financial system began to totter. In order to prevent complete collapse, Germany instituted a rigid control of her foreign exchange, obtained a "standstill" agreement with her short-term creditors delaying the withdrawal of funds, sought and secured a postponement of reparation payments and imposed further restrictions upon imports. Standstill agreements and similar measures were applied in other Central European countries. Following these events the financial crisis shifted to London.

The overvaluation of sterling and Britain's declining share of world trade had progressively weakened her financial position. Partly as a result of this condition London was both a large borrower and lender of short-term funds. As the general uneasiness became acute, foreign deposits were rapidly withdrawn from London. These withdrawals were possible only so long as British loans in Central Europe could be liquidated. When these became "frozen" the drain could no longer be met and the pound was forced off the gold standard. The British abandonment of gold in September, 1931, was temporarily at least, a severe blow. Credit conditions tightened everywhere and international lending ceased altogether. The sharp fall in the gold value of the monetary unit of the biggest import market in the world pushed prices in terms of other currencies, particularly prices of foodstuffs and primary commodities, further down the deflationary spiral. The pressure on debtor countries and on exporters of raw materials and agricultural commodities was intensified. This brought another wave of nationalistic measures to protect the exposed economic and financial structures against collapse. Many of the countries which had close economic relations with Great Britain, namely the Scandinavian countries, most of the British Empire, Egypt and Portugal, followed her off the gold standard immediately. Between September, 1931 and the middle of the next year, seventeen countries departed from gold. Nearly thirty countries established controls over their foreign exchanges. The disorganization of international finance and the continued decline in gold prices were accompanied by an increase in restrictions to trade. In addition to the raising of tariffs

in nearly every country on the globe, there was a virtual stampede in the adoption of import quotas, licensing systems, import monopolies, milling regulations, etc. Great Britain, long the stronghold of free trade, succumbed to a system of moderate protection. Under the growing paralysis caused by these measures the value of international trade fell precipitously. The economic world lay prostrate and apparently helpless under a succession of disasters.

By 1933 the value (in terms of pounds sterling) of world trade had fallen nearly 50 per cent from the level of 1929. About half of this contraction was due to the fall in prices and half to the shrinkage in volume. These decreases, because of their nature, fell with particular severity upon the debtor countries and the exporters of primary commodities. In order to maintain solvency supplies were pressed upon the export markets intensifying the disproportionate decline in prices. The volume of world trade of foodstuffs and raw materials dropped only 15 per cent, compared with a decrease of 40 per cent in manufactures. The prices of the former, however, fell about 15 per cent lower (from 1929) than the latter. The effects upon agricultural exporters of import restrictions and the attempts to attain self-sufficiency are illustrated by the fact that, while in 1933 the total world production of foodstuffs was slightly greater than in 1929, world trade in these commodities had fallen by nearly a fifth. The agricultural crisis together with the strangulation of trade and the widespread dislocation of the international exchanges were the major factors contributing to the unusual severity of the depression. At the bottom of the decline world industrial production had fallen 37 per cent from 1929. Three out of every ten of the world's industrial wage-earners were out of work.

Recovery—failure of international efforts and intensification of economic nationalism

It seemed to be impossible to overcome the international economic anarchy which so intensified and prolonged the slump. The failure of the World Economic Conference of 1933 emphasized the apparent futility of the attempts to promote recovery through international co-operation. Each country turned to its own national policies to bring about economic revival. Everywhere defences were thrown up to shield the national economies against depressing or limiting external influences. Great Britain sought to stimulate recovery by a policy of easy money behind an exchange depreciated

against the gold bloc, encouragement to home investment by the restriction of foreign and governmental assistance to housing, moderate protection to industry and protection and subsidies to agriculture. The Scandinavian countries and the British Dominions likewise tried to promote easy money, price raising and investment, behind depreciated exchanges and greater restrictions against imports. The United States endeavoured to raise the internal price level by increasing the price of gold; to remove the disparities between agricultural and industrial prices by restricting farm output to domestic requirements; to spread employment and raise wages by shortening hours, regulating competitive conditions, and strengthening the power of organized labour; to promote investment by credit expansion and easy money; and to increase consumers' purchasing power by a gigantic program of government spending. In contrast to the expansionist policies of the nations with depreciated currencies, the gold bloc countries (chiefly France, Switzerland, Belgium and the Netherlands) attempted the vigorous program of deflation demanded by the maintenance of the gold standard. As the deflation continued confidence waned, the depression deepened and tariffs, import quotas and import licences became more and more exclusive. The restrictive measures proved unsuccessful and eventually expansionist policies were adopted which forced the bloc to abandon the gold standard in 1936. The Central European countries, particularly Germany and Italy, used the methods of the totalitarian state to increase employment and to expand economic activity. Exchanges were rigidly controlled; imports were rationed; prices and wages were fixed; profits were limited; the direction of investment and industrial expansion were dictated by the state; huge public works and armament programs were undertaken.

While the devices of national self-help were being employed to hasten readjustments and to promote recovery in individual countries, international efforts were put forth to improve the position of the raw materials which were sold on world markets. Old schemes were revived and new ones started, in some cases under the aegis of the governments concerned and in others merely by direct agreement among the producers. Eventually, nearly every important commodity was subject to some form of control. The newly constituted schemes generally had greater control over total output than those of the past and hence were able to achieve their objectives without the same unfortunate con-

sequences. Thanks to rising demands they were able to work off surplus stocks and to engineer a considerable rise in prices. However, very few international difficulties were so smoothly overcome. The agricultural depression was relieved temporarily only by a succession of disastrous droughts in North America. The most pressing problems of international indebtedness were solved mainly by arbitrary and unilateral methods. A number of countries in Latin America and South Eastern Europe suspended the services on their external debts. The large inter-governmental payments on account of War debts were defaulted. The attempt to collect reparations had to be finally abandoned.

The national efforts, the reduction in the weight of unproductive debts, and to some extent the restriction schemes achieved a considerable success in promoting recovery. Expansionist policies and easy money helped to raise prices; inventories were depleted, capital equipment had worn out and needed replacement, technical improvements accumulated, costs were reduced, the buying of durable consumers' goods revived in the United States and an armaments boom got under way in Europe.

Economic Isolationism and Self-Sufficiency—reduced importance of world trade and unfavourable circumstances of debtor countries and exporters of foodstuffs

In 1937 world industrial production was greater than and world industrial employment was about equal to that of 1929. The price disparities between agricultural products and raw materials on the one hand and manufactured goods on the other had disappeared. However, during the eight years the structure of the world economy had changed significantly. The level of economic activity in Germany, Great Britain, Sweden and Japan was from 15 per cent to 40 per cent higher than in 1929, whereas in the former gold bloc countries, the United States, and Canada it was still slightly lower. While world manufacturing production and the production of industrial raw materials were nearly 20 per cent greater than the pre-depression peak, agricultural production was only 7 per cent greater; the production of non-ferrous metals was 21 per cent greater; wood-pulp 38 per cent greater; electricity 47 per cent greater. The new age of alloys, plastics, and synthetic textiles brought new industries and areas to the fore and left others mired in the depression.

By 1937 total world production was considerably above that of 1929, but the volume of world trade was slightly lower. The divergence between world production and trade was particularly pronounced in the case of foodstuffs and manufactured goods. The world exports of wheat were one-third less and those of finished articles about one-sixth less. The absence of international lending, the heightening of trade barriers as defences against depression and the emphasis upon national efforts to promote recovery, reduced the importance of foreign trade in the world's economic life. This tendency was intensified by the struggle for self-sufficiency which arose out of the deterioration of political relations between nations and the fear of war. The heavy expenditures on armaments reduced the amount of foreign exchange available for imported foodstuffs and other consumers' goods. The choice between "guns or butter" was dictated first to the nations as a whole and then to their individuals. The universal limitation to standards of living, which was involved in the efforts to attain national security, and military power, fell with particular severity upon those who had the greatest stake in the advantages of international economic co-operation—the countries with an overwhelming dependence upon a few specialized exports.

2. THE INCIDENCE OF THE DEPRESSION ON CANADA
Impact of World Depression—its full force falls upon Canada's staple exports; the drastic slump in agricultural and raw material prices

The implications of the nature and extent of the world depression to Canada are obvious. The effects upon this nation, which obtains over one-third of its national income directly from abroad and two-thirds of whose exports consist of raw materials, were extremely drastic. For upwards of thirty years external influences and technical changes had played favourably upon Canada's resources and produced an era of almost unbroken expansion and prosperity. The Canadian economy had become delicately geared to the increasing foreign markets for foodstuffs, newsprint, lumber and minerals. For the production of these commodities a large and expensive transportation system was built and huge amounts were invested in power projects, processing plants, implements and machines. Much of the capital required for the provision of this immense equipment was borrowed from other countries. The application of this capital and of advanced techniques to virgin resources became the principal basis of our economic life. It involved a narrow specialization in the

production of a few export staples, heavy fixed charges, and a precarious dependence upon the commercial policies of other countries.

As long as the conditions of international trade were favourable, specialization yielded a high standard of living and heavy commitments were undertaken with great confidence. Our social and economic institutions became closely related to the nature of the economy and rested on the condition of continuous expansion. When the bases for progress along the old lines disappeared and the full force of the world depression fell upon our specialized exports, the problems of adjustment were extremely difficult. Canada's political, public finance and economic organizations were not adapted to deal with sharp and prolonged economic reverses. When a specific and co-ordinated program was required, there was bewilderment; when positive action was needed there were only temporizing and negative policies; when a realization of the far-reaching effects of the altered circumstances was demanded, there was but faith in the speedy return to the old conditions of prosperity.

The general vulnerability with which Canada entered the world depression was intensified by a number of particular circumstances. The market situation for the two leading exports, wheat and newsprint, was especially weak. The unusually large world and Canadian wheat crops of 1928 created a burdensome surplus which threatened a slump in prices even before the depression began.¹ As world agriculture was rapidly approaching a crisis, this factor was particularly menacing. By 1929 Canadian newsprint capacity was over-extended and the price situation was very unstable. Since Canada supplied 40 per cent of the world exports of wheat and 65 per cent of the world exports of newsprint, she would suffer the full impact of unfavourable developments.

In addition to the dark outlook for the two principal exports, there was the over-extended condition of the internal credit structure. Canada was closely affected by the investment and speculative boom in the United States. Her citizens participated extensively in the New York stock market and assumed large capital commitments with typical North American optimism. These tendencies were facilitated by the nature of the Canadian monetary system which was without

¹ Between August 1, 1928 and August 1, 1929 the world wheat carryover rose from 697 million bushels to 957 million bushels.

anchor and without control.² Under the Finance Act the Canadian banks were able to extend their loans and increase the money supply without reference to the restrictions of the gold standard, which in fact had to be abandoned as early as the end of 1928. Consequently, in the atmosphere of the time, credit was over-expanded giving rise to much speculative and inflationary activity. Wage-earners were thus drawn into the capital goods industries in undesirably large numbers and when the depression struck the problem of unemployment and the shock to confidence was all the more severe.

The decline in world economic activity and prices was immediately communicated to Canada and her weaknesses were quickly exposed.

TABLE 41.—THE DECLINE IN EXPORT PRICES AND ECONOMIC ACTIVITY, 1929-33

—	The Prices of 17 Major Exports	Export Prices of Farm Products ^(a)	All Wholesale Prices	Index of Employment ^(b)	Index of Industrial Production ^(c)
1929 July.....	100	100	100	100	100
1930 June.....	82	70	90	93	80
1930 December	66	42	80	87	74
1931 June.....	62	42	74	83	64
1931 December	61	41	72	80	61
1932 June.....	54	37	63	72	59
1932 December	47	30	66	67	52

^(a) Includes Wheat, Barley, Potatoes, Cheese, Bacon and Cattle.

^(b) Dominion Bureau of Statistics Index of Employment.

^(c) Dominion Bureau of Statistics Index of Industrial Production.

It was the sharp fall in export prices which pushed Canada down the incline of depression. The level of export values was directly the basis of the income of a large section of the economy; it determined the incentives for capital investment and the size of the market for the protected manufacturing industry. When these values shrank, the repercussions were widespread. In twelve months (January, 1930 to December, 1930) the average of the prices of 17 major exports fell 30 per cent; wheat was down 57 per cent, cattle 36 per cent, copper 38 per cent, dried codfish 31 per cent, and lumber 20 per cent. The factors which were responsible for these sudden and drastic declines became increasingly unfavourable as the

² "An examination in the light of contemporary conditions of the rates charged from time to time on Finance Act advances suggests that these rates were not used as an instrument of credit expansion and contraction, but were mainly varied to meet the exigencies of the Dominion Government's finances. The volume of advances was not subject to the restriction of a gold reserve. The Treasury Board did not assume the responsibility of ensuring that the uses made of the Finance Act were consistent with the requirements of a convertible currency. The banks, on the other hand, which could take the initiative of expanding the credit base through advances of Dominion notes under the Finance Act, were under no obligation to use this initiative in maintaining the gold standard. Thus the Finance Act did not provide Canada with the organization needed to undertake the tasks which the maintenance of the restored gold standard implied." *Report of the Royal Commission on Banking and Currency in Canada, 1933, p. 69.*

world depression deepened. Agricultural products particularly were dealt a succession of hard blows. In 1930 the German, Italian and French tariffs against wheat were raised to the prohibitive levels of \$1.62, \$1.07 and \$0.85 per bushel respectively. Later such duties were supplemented by all manner of quantitative restrictions which almost completely closed these important markets and decreased the export outlets by upwards of 150 million bushels a year. During 1930 the currencies of Canada's principal competitors in the wheat market, Australia and Argentina, began to depreciate rapidly. When Britain abandoned the gold standard and the monetary unit of the largest purchaser of wheat went to a discount in terms of Canadian dollars, Canada's disadvantages were intensified. By the end of 1932 the Australian pound and the Argentine peso were 46 per cent and 40 per cent, respectively, below their former gold parities. Furthermore, during 1930-32 Russia suddenly pushed large supplies of wheat into the world market, the Danubian countries began to subsidize exports, and the United States Federal Farm Board started to unload its stabilization holdings. In December, 1932 the Winnipeg wheat price fell to 38 cents per bushel, the lowest in history. The agricultural problem was generally aggravated by the Hawley-Smoot Tariff of 1930. During the twenties an important export business in cattle and potatoes, and a border trade in milk and cream was done with the United States. The new tariff rates put an end to these and the surplus production flooded the domestic market.³ By February, 1933, the average of all Canadian farm prices had fallen nearly 60 per cent from 1929.

Primary products other than those of agriculture suffered similar, if not quite such drastic, price declines. The producers of lumber were especially affected by the sharp curtailment in construction activity. Furthermore, the free entry of lumber into the United States was terminated by the tariff of 1930 and the high duty imposed by the Revenue Act of 1932.⁴ In the British market the Canadian exporters faced increasing competition from Russia and the Baltic countries, which with the depreciation of their currencies after 1931, had an exchange advantage.

As in the case of lumber, the exports of base metals were heavily dependent upon the world boom in capital investment. When this boom broke and the buying of automobiles and electrical appliances was abruptly curtailed, the consumption of these metals dropped precipitously.⁵ At the same time, a large amount of new, low-cost, productive capacity arising from projects initiated earlier, and based on improved processes and new discoveries, was just coming into operation. The cartels were unable to control output, stocks piled up and prices slumped disastrously. The 4 cents per pound duty on copper, imposed by the United States in 1932, depreciated currencies, and the efforts of European countries to promote domestic production by means of tariffs, quotas and subsidies, contributed to the unfavourable circumstances. Canada, however, was in a relatively advantageous position. She had a virtual monopoly of nickel and a fixed price was maintained. Nearly all the copper, lead and zinc were produced as by-products of nickel, gold or silver, or vice versa. Furthermore, a number of large capital programs for new and extended mining and refining operations involving the latest low-cost processes were just being completed as the depression broke. Nevertheless, with the fall in copper, lead, zinc and silver prices to less than half of the 1926-29 averages, export values contracted sharply.

In the case of newsprint, 85 per cent of the market was in the United States where the depression was particularly severe. Between 1929 and 1933 United States consumption of newsprint fell 30 per cent while Canadian productive capacity increased by nearly 20 per cent. Under the peculiar conditions of the newsprint market and the financial organization of the Canadian newsprint industry these changes wrought havoc with the price structure. On the supply side there were relatively few and unorganized producers, each with a heavy bonded debt, to whom the maintenance of volume was extremely important.⁶ The demand side was dominated by a few powerful organized buyers whose requirements were decreasing. The sellers had to keep up output in order to meet the large fixed charges and avoid bankruptcy. The buyers took advantage of this situation and because of mutual distrust and divergent interests, the Canadian producers were unable to maintain a united front against the united pressure of the buyers. Consequently, the price tended to be forced down

³ Between 1929 and 1933 the exports of cattle to the United States fell from \$13,800,000 to \$400,000, of milk and cream from \$1,700,000 to \$40,000, and of potatoes from \$3,800,000 to \$700,000. These declines were partially due to the general fall in prices and the decrease in United States consumption, but the higher tariffs were undoubtedly the main cause.

⁴ The exports of Canadian lumber and timber to the United States dropped from \$28.6 million in 1929 to \$13.1 million in 1933.

⁵ Between 1929 and 1933 the world consumption of nickel fell 52 per cent, of copper 48 per cent, of lead 37 per cent, of zinc 42 per cent.

⁶ Even at the 1933 price the industry had to operate at 80 per cent of capacity in order to meet its full interest charges.

to the out-of-pocket operating costs leaving little or no margin for fixed interest charges. In 1933 the Canadian newspaper industry was working at 53 per cent of rated capacity, the price ⁷ had fallen nearly 40 per cent (from 1929), and seven companies representing 50 per cent of the total Canadian capacity had defaulted on their indebtedness and were bankrupt.

The depression added greatly to the unfavourable circumstances which have long harassed the Atlantic fishing industry. Beginning in 1930 the world's largest importers of dried cod, Spain, Portugal and Italy, imposed prohibitive trade restrictions which severely curtailed consumption. The purchasing power of Canada's important outlets in the Latin American countries, which was tied to coffee and sugar, was drastically reduced.⁸ In these markets there was also increasing competition from the subsidized exports from Europe and from the British, Norwegian and Icelandic producers whose currencies had depreciated further than the Canadian dollar. The trade agreement (1926) with the British West Indies was of little assistance to the Nova Scotia fishermen since Newfoundland enjoyed the same preferences. Furthermore, this treaty which transferred Canadian sugar purchases entirely to Empire sources,⁹ practically closed Canada's important outlet for fish in Cuba. The fresh fish trade with the United States and Central Canada suffered considerably from the low prices for substitute foodstuffs, meat, eggs and dairy products. At the bottom of the depression the average of the export prices of Canadian fish was cut in half; the price of dried cod was down nearly 70 per cent.

By 1933 the average of all Canadian export prices (except gold) had fallen 40 per cent from 1929. This drop was nearly one-fifth greater than the fall in the cost of imports and 10 per cent greater than the fall in the general wholesale price level. The important staples of agriculture and Atlantic fisheries suffered the most drastic declines.

TABLE 42.—CANADIAN EXPORT PRICES, 1929-33

—	All Exports (ex. gold)	Wheat	Cattle	Lumber	Newspaper	Copper	Dried Cod-fish
1929..	100	100	100	100	100	100	100
1930..	84	70	87	87	100	75	82
1931..	66	44	59	75	91	50	56
1932..	60	41	46	67	79	38	44
1933..	60	45	37	68	62	44	42

⁷ F.a.b. Canadian mills.

⁸ Between 1929 and 1933 the exports of raw sugar from Cuba fell from \$178 million to \$39 million, and coffee from Brazil fell from \$327 million to \$127 million.

⁹ The sugar preferences in the British West Indies Treaty were extended to the other Empire countries.

Effects of Severe Decline in Export Prices—sharp increase in burden of external interest payments, increase in real cost of imports, and drastic curtailment of construction activity

The result of the steep fall in export prices was, of course, to reduce sharply Canada's income from abroad. This reduction, aside from its other far-reaching effects, greatly increased the burden of external obligations. The Canadian economy was like a huge bonded corporation in which the export producers held the equity interest. The large amount of capital required (for railways, canals, power plants, community equipment and factories) for the most profitable exploitation of its domain was most rapidly obtained by the sale of bonds to foreigners. The first charge on the income (exports) consisted of the interest on this bonded debt; the export producers received what was left and, therefore, this remainder rose and fell with the corresponding changes in export prices but at a much faster rate. Hence it was very large when prices were high and extremely small when prices were low. Those farthest out on the long arm of this lever were the farmers, the fishermen, the lumbermen and the miners, in whose rigid costs (freight rates, taxes, mortgage interest and cost of equipment) the fixed interest charges were expressed.

In 1930 about 40 per cent of all the capital invested in Canadian business (excluding farms) and government securities was owned abroad. Over one-half of this total Canadian capital was in the form of bonded debt of which about two-fifths was held in Great Britain and foreign countries. Since the residents of other countries had provided such a substantial part of our total capital, they naturally had a substantial claim on our total income. These claims could be met only by the exports of goods and services, the prices of which would determine the weight of the burden. At the bottom of the depression this burden had increased by 40 per cent. In 1928-29 external interest obligations and dividends absorbed less than one-sixth of the total receipts from the exports of goods and services; in 1932-33 they took one-third. During the former period over \$1,500 million was left annually after interest and dividend payments; in 1932-33 this had fallen to less than \$580 million. Canadians had lost one billion dollars of income from abroad with which they formally bought goods and services from other countries. Furthermore, the real cost of foreign goods had risen. In 1933 nearly one-fifth more of Canadian exports were required to buy the same quantity of imports as in 1929.

TABLE 43.—CANADIAN PAYMENTS AND RECEIPTS FROM ABROAD^(a)
(Millions of Dollars)

	PAYMENTS ABROAD				RECEIPTS FROM ABROAD				
	Interest and Dividends	Net Capital Exports	Available for the Purchase of Commodities and Services	Total Payments ^(c)	Total Receipts ^(c)	Monetary Gold + Export - Import	Net Capital Imports	Receipts from Commodity Exports and Tourists ^b	Receipts from Investments Abroad Freight and Other
1928.....	274	82	1,530	1,886	1,930	+ 49	—	1,671	210
1929.....	322	—	1,639	1,961	1,933	+ 37	168	1,516	212
1930.....	348	—	1,276	1,624	1,653	- 36	315	1,163	181
1931.....	330	—	826	1,156	1,116	+ 33	36	902	145
1932.....	301	11	610	922	891	+ 3	—	775	113
1933.....	263	32	559	854	844	+ 6	—	731	107

^(a) Compiled from *The Canadian Balance of International Payments, 1939*, The Dominion Bureau of Statistics, Tables 40-51.

^(b) Includes exports of non-monetary gold.

^(c) The differences between total receipts and payments are due to errors and omissions in the estimates.

An immediate effect of the slump in export prices was the drastic curtailment of construction activity. A large part of the capital investment of the twenties was directly concerned with increasing the capacity and efficiency of the export industries, i.e., railways, hydro-electric power, pulp and paper plants, development of non-ferrous metal mines, etc. When the profitability of these industries was sharply reduced the incentives to embark on new ventures disappeared. The value of construction contracts awarded in 1933 was one-sixth as large as in 1929 and nearly two-thirds of the thousands of workers formerly engaged in construction were out of work.

Great Disparities in Incidence of Depression—burden fell on unemployed, primary producers and investors in equities; effects of immobility, specialized activity, rigidities of interest and wages, monopolistic conditions, tariffs

The impact of the loss of export income fell most directly upon the export producers and the construction and engineering trades. From these it spread in widening circles throughout the economy.

The manner in which the losses were distributed, however, was anything but uniform. The unequal incidence of the burden on the different groups and regions in the country was the outstanding feature and the basis of the most serious problems arising out of the depression. The extent to which the disturbances in one sector of the economy may be

shifted to others depends upon the flexibility of prices and costs and the mobility of labour and capital. In these respects the Canadian economy is highly rigid. Canadian economic life rests on the specialized exploitation of a few natural resources whose products are exchanged in the international market for the many manufactures, raw materials, and services which enable Canadians to enjoy a high standard of living. When the export markets shrink the climate and limited variety of resources preclude the development of alternative occupations. The huge amounts of capital in the export industries cannot be transferred to other uses. Furthermore, much of the capital is in the form of fixed commitments. Over one-fifth of all the capital in Canadian private industry is bonded debt. Nearly 30 per cent of the capital invested in the farm property of the Prairie Provinces is money borrowed in one way or another at contractual interest rates. In addition there are the outstanding debts of Canadian governments which amount to the substantial figure of \$707 (1937) per capita. Altogether Canadian industry and governments have to meet a fixed interest bill of about \$500 million annually. The decline in the cost of living substantially increased the real value of such fixed interest payments but none of the depression burdens could be shifted (except by taxation on a national scale) to the recipients of this income without default and bankruptcy.¹⁰

¹⁰ Reductions in interest charges are possible by refunding and voluntary conversions but these are dependent upon special circumstances and usually take place with a considerable lag.

TABLE 44.—FIXED INTEREST CHARGES AND THE NATIONAL INCOME, 1929-33

	The National Real Income ^(a)	The real value of the average rate of interest paid on Government debt ^(b)	Bond interest and interest on farm mortgages received by Canadian individuals as a percentage of the National Income ^(c)	Bond interest and interest on farm mortgages received by Canadian individuals and paid abroad as a percentage of the National Income ^(c)
	1929 = 100	1929 = 100	%	%
1929.....	100	100	3.1	6.5
1930.....	89	100	3.8	7.9
1931.....	83	108	4.5	9.6
1932.....	74	119	5.6	11.6
1933.....	72	123	6.2	12.6

^(a) The indices of the national money income divided by the Dominion Bureau of Statistics indices of the cost of living.

^(b) The indices of the average rate of interest paid on the outstanding debts of the Dominion and the provinces, divided by the Dominion Bureau of Statistics indices of the cost of living.

^(c) Includes investment income of life insurance companies accruing to policy holders.

While fixed interest charges are an onerous burden during periods of declining values, rigid wage rates are perhaps far more productive of strains and dislocations since they comprise a much larger share of the total cost of production. Wage rates and salaries, particularly in the skilled and semi-skilled trades and professions, have everywhere become extremely inflexible. The maintenance of wages during periods of shrinking purchasing power resulting from the fall in export incomes or the collapse of investment means that prices cannot be reduced to the levels at which the product of industry at full employment may be sold. The necessary adjustment is, therefore, made by a reduction in the volume of output which deprives a large number of workers of their jobs. Thus the burden is thrown on the unemployed, who have completely lost their income, and on the primary producer, the prices of whose products have fallen sharply, while the things he purchases (services and manufactured goods) have not.

On the average, employed wage-earners and persons receiving salaries suffered no reduction in real income. Most of the workers in the skilled trades, the professions and the white-collar occupations who retained their jobs actually enjoyed a considerable improvement in their real position. The losses were completely borne by the 500,000 to

TABLE 45.—THE INCIDENCE OF THE DEPRESSION, 1929-33

	The National Real Income per capita ^(a)	Real wages, mainly in the skilled trades ^(b)	Average annual real salaries and wages received by all employed wage-earners ^(c)	Number of unemployed wage-earners ^(d)	Purchasing power of farm products in terms of manufactured goods	Real value of dividends received by stockholders ^(e)
	1929 = 100	1929 = 100	1929 = 100	(000)	1929 = 100	1929 = 100
1929.....	100	100	100	107	100	100
1930.....	87	101	97	241	87	111
1931.....	81	108	102	442	70	102
1932.....	71	111	105	659	64	77
1933.....	68	111	102	646	67	78

^(a) Indices of the national money income per capita divided by the Dominion Bureau of Statistics indices of the cost of living.

^(b) Dominion Department of Labour indices of wage rates divided by the Dominion Bureau of Statistics indices of the cost of living.

^(c) Annual average salaries and wages were obtained by dividing total salaries and wages paid out as estimated in the Commission's study on National Income by the total number of wage-earners employed receiving salaries and wages as estimated by the Dominion Bureau of Statistics. (*Canada Year Book*, 1939, p. 812). The resulting averages were converted to indices and divided by the Dominion Bureau of Statistics indices of the cost of living.

^(d) Dominion Bureau of Statistics estimates, *Canada Year Book*, 1939, p. 812.

^(e) Indices of dividends paid to Canadian stockholders by Canadian and foreign corporations, divided by the Dominion Bureau of Statistics indices of the cost of living.

600,000 unemployed who depended on past savings and private or government charity, by the farmers and other primary producers, and by the investors in common stocks, and others who received the profits of industry and trade.

While fixed interest charges and the inflexibility of wages were important factors in the rigid prices and costs which spread the losses of the depression so unequally, they were by no means the only ones. Business organization has everywhere become increasingly monopolistic. In Canada industry, commerce and finance are highly centralized and in many branches a few enterprises dominate the field. Under such conditions the maintenance of prices is possible in the face of declining demands. The monopolistic producers may consider that they are better off by selling less at higher prices than by selling more at lower prices. Consequently, the burden tends to fall upon the workers who lose their jobs through the reduction in output and on the exporters whose costs are thus held rigid while their prices on world markets are sharply reduced.

An important condition of monopolistic practices and of the rigidity of certain prices is the absence of foreign competition. Such competition is limited mainly in two ways: artificially, by protective tariffs and import regulations; naturally, by the costs of

transportation and the necessity for rendering the services or producing the commodities on the spot as in the case of trade, banking, professional services, government services, the production of bread, milk, etc. Industries which are artificially or naturally sheltered, selling only or principally in the domestic market, can adjust their prices to costs, whereas the exporters have to adjust their costs to the prices they can get on the world market. Since the prices of the protected industries determine in part the costs of the exporters, it is clear that the latter are in an unenviable position.

The Canadian manufacturing industry, except that portion of it engaged in the processing of export staples and certain naturally sheltered branches, grew up behind a protective tariff. The steep increase in duties during 1930 and 1931 and the intensification of administrative restrictions greatly widened the scope for the maintenance of prices. The exporter and the raw material producer could get little relief from a reduction in costs forced by external competition.

TABLE 46.—INDICES OF SHELTERED AND EXPOSED PRICES
1929 = 100

	Cost of Living ^(a)	Prices of Tariff Protected Manufactured Goods ^(b)	All Wholesale Prices ^(c)	Export Prices ^(d)	Farm Prices ^(e)
1929.....	100	100	100	100	100
1930.....	99	98	91	84	83
1931.....	90	83	75	66	56
1932.....	81	66	70	60	48
1933.....	78	65	70	60	51

^(a) Dominion Bureau of Statistics Indices.

^(b) Includes all iron and steel products, manufactured textiles, boots and shoes, chemicals and allied products, glass and its products, cement, gasoline and pottery.

The higher tariffs imposed early in the depression were effective in diverting an important part of total demand from the foreign to the home producer. Consequently the Canadian manufacturer had a considerable cushion against the contracting market. Total salaries and wages in the tariff-protected manufacturing industry fell proportionately much less than earnings in many other occupational classifications.

The naturally sheltered industries and occupations were even more thoroughly shielded against the losses of the slump. The costs of many professional and personal services, and of the distributive and administrative overhead of the

country, could not be sharply reduced. With the decline in the cost of living, most of those engaged in these services were better off in 1933 than in 1929. Far from assuming any considerable part of the depression burdens, they received a considerable increment in their share of the national income.

TABLE 47.—THE UNEQUAL INCIDENCE OF THE DEPRESSION
ON THE EXPOSED AND SHELTERED GROUPS, 1929-33

	Net Income of Farmers as a percentage of National Income ^(a)	Salaries and Wages in Selected Export Industries as a percentage of National Income ^(b)	Sub-total Exposed Industries	Salaries and Wages in Manufacturing mainly dependent on Tariff Protection as percentage of National Income ^(c)	Salaries and Wages in the Naturally Sheltered Industries and Occupations as a percentage of National Income ^(d)	Sub-total Sheltered Industries
1929.....	15	8	23	14	29	43
1930.....	16	8	18	15	31	46
1931.....	6	7	13	16	33	45
1932.....	5	7	12	15	35	50
1933.....	7	7	14	15	35	50

^(a) It should be noted that an important cause of the steep decline in agricultural income was the drought in the Prairie Provinces. However, in 1932, when agricultural income reached its lowest point, the crop on the Prairies was the second largest in history.

^(b) Includes salaries and wages in agriculture, logging, primary mining, flour mills, fish curing and packing, pulp and paper, saw-mills and non-ferrous metal smelting and refining.

^(c) Salaries and wages in all manufacturing, excluding central electric stations and the industries included in ^(b).

^(d) Includes salaries and wages in transportation and communication, merchandising, government and education, banking, insurance and the professions.

Another important influence determining the incidence of the depression was the differing behaviour of the demand for capital and consumers' goods. One of the main factors in the collapse of the boom was the sharp curtailment of construction activity. The undertaking of large projects virtually disappeared, and the building of houses, the purchase of machinery and equipment, and normal maintenance and repair expenditures, were drastically reduced. In the psychological atmosphere of the depression everything that was not immediately necessary was postponed. Hence the industries producing the goods required for capital investment suffered a severe reduction in demand. On the other hand, the consumption of food, clothing, fuel, etc., could not be substantially cut down regardless of the uncertainty, lack of confidence or shrinkage of income. The industries producing consumers' goods were thus able to maintain a relatively high level of output. The

closer the industry is to supplying the basic necessities of life, the more constant is the demand. At the other extreme, consumer buying of luxuries, semi-luxuries and durable goods such as furniture, automobiles and electrical appliances, is almost as unstable as investment. The greater the proportion of the national income which is devoted to the purchase of the latter classes of commodities, the greater are the possible economic fluctuations. Canada, with her high standard of living, was especially vulnerable in this respect. On the whole, however, the consumers' goods industries bore relatively little of the depression burdens.

TABLE 48.—INDICES OF THE PRODUCTION OF CONSUMERS' AND PRODUCERS' GOODS, 1929-33

	Consumers' Goods ^(a)	Producers' Goods, (mainly capital goods) ^(a)
1929.....	100	100
1930.....	93	83
1931.....	89	62
1932.....	82	46
1933.....	84	48

^(a) Dominion Bureau of Statistics Indices.

Disparities in Incidence of Depression on Different Regions—loss of income most severe in Western Canada, declines range from 72 per cent in Saskatchewan to 36 per cent in Nova Scotia

The incidence of the depression on the various regions and provinces was determined by their relations to the factors discussed above. Owing to the rigidity of wages, fixed interest charges, monopolistic practices, the effects of protective tariffs, the importance of highly specialized activity, and the immobility of capital and labour, there was no reason to expect anything approaching a uniform distribution of losses.

The depression burdens which could be shifted only with great difficulty, in the end fell almost completely on the exporters, the unemployed, the investors in defaulted farm mortgages, and the receivers of income from equities. In Central Canada and Nova Scotia, where the amounts obtained from salaries and wages in tariff-protected and naturally sheltered occupations and from fixed interest investments were relatively the greatest, the total incomes fell least. In Western Canada, where the proportions of the receipts from export

TABLE 49.—DEPRESSION DECREASES IN NET MONEY INCOME

	Percentage Change 1932-33 Average Income from 1926-29 Average Income
	%
Agriculture—Prairies.....	- 94
Fisheries.....	- 72
Salaries and Wages in Construction.....	- 68
Agriculture—Eastern Canada and British Columbia	- 64
Salaries and Wages in the Exporting Industries ^(a)	- 60
Total National Income.....	- 41
Dividends received by Stockholders.....	- 40
Salaries and Wages in the Protected Manufacturing Industries ^(b)	- 37
Income of Small Business men and the Professions—Individual Enterprisers.....	- 36
Salaries and Wages in the Sheltered Occupations.....	- 30
Miscellaneous Income ^(c)	- 18
Bond Interest, Property Income from Life Insurance and Interest on Farm Mortgages received by Individuals.....	+ 13

^(a) Includes salaries and wages in agriculture, logging, primary mining, flour mills, fish curing and packing, pulp and paper, saw-mills and non-ferrous metal smelting and refining.

^(b) Salaries and wages in all manufacturing excluding central electric stations and the industries included in ^(a).

^(c) Includes net income from urban housing and municipal public welfare and education.

production were the highest, the total incomes fell most. The Prairie Provinces, almost wholly dependent upon the export of wheat, suffered the most severe declines.

TABLE 50.—THE DECLINE IN PROVINCIAL PER CAPITA INCOMES, 1928-29 TO 1933

	1928-29 average \$ per capita	1933 \$ per capita	Percentage Decrease
Saskatchewan.....	478	135	72
Alberta.....	548	212	61
Manitoba.....	466	240	49
Canada.....	471	247	48
British Columbia.....	594	314	47
Prince Edward Island.....	278	154	45
Ontario.....	549	310	44
Quebec.....	391	220	44
New Brunswick.....	292	180	39
Nova Scotia.....	322	207	36

The large disparities shown in the above table are striking testimony of the extreme differences in the incidence of the depression and of the great problems of public finance and economic policy which they created.

3. THE NATIONAL ECONOMIC POLICIES DURING THE DEPRESSION

The policies of the Dominion had played a significant part in determining the direction of Canadian economic development and in shaping the structure of the economy. The costs and markets in every region and industry in the country had been basically affected by the conditions of transportation and by the protective tariff. The nature and operation of these policies were obviously important factors in the incidence and course of the depression.

The policies of Western settlement, all-Canadian transportation, and industrialization by protective tariffs had been designed to promote, and to function under the influences of, expansion. They had set the stage and in some measure had provided the incentives for the activities of private enterprise which were counted on to bring general prosperity and build an economically integrated and united nation. The success of the whole scheme depended upon the availability of extensive virgin resources and expanding foreign markets. In 1930 when the external influences became extremely unfavourable and the supply of new land suitable for agriculture had become virtually exhausted, the old policies became largely negative. They were important conditions under which the economy had grown up and under which individuals had obtained their opportunities and produced their incomes and thus could not be sharply reversed without severe repercussions. On the other hand, the nation's prosperity could no longer be maintained simply by settling immigrants and subsidizing the construction of railways.

The depression brought a set of problems almost entirely new in Canadian experience. Their solution or amelioration required new departures in federal policy. Broadly there were two alternatives. One was to try to counteract the factors which were responsible for the slump by attempting to maintain export values, to keep up activity in construction, and to prevent prices and costs from getting too far out of line. This would have involved what then appeared to be risky and unorthodox monetary measures. The other was carefully to avoid risky and unorthodox monetary measures and to endeavour to maintain income in the sheltered and protected sectors of the economy by drastic restrictions against imports, by following "sound" financial policies which would maintain confidence, preserve the public credit both internally and abroad, and thus facilitate the operation

of the natural forces of recovery. While there could be no absolute certainty about which course would hold the total national income at the higher level, the latter would widen the disparities in the losses falling on the various groups (because of the relative increase in exporters' costs, the increase in disparities between price levels and the harmful effects on foreign markets) and hence would greatly increase the transfers of income which would have to be made through the public finance system to support the casualties of the unequal incidence of the depression. The second alternative describes briefly the policies which were actually adopted by the Dominion.

Monetary policy—difficulties and uncertainties of currency management in Canada, maintenance of equilibrium in balance of payments by tariff and orthodox monetary policies, failure to shield exporters against drop in external prices

The failure to take any positive steps to soften the impact upon the exporters or to forestall the wide disparities which developed arose to a considerable extent out of the economic difficulties and uncertainties which were involved. It must be emphasized that this review is made with the wisdom of hindsight. It is obvious that after the event many things become clear which were not so before. The most direct and general attack on the problem was in the field of monetary policy, where the issues, at least at that time, were particularly obscure. Should the country in the confident security of monetary orthodoxy undergo the full effects of a deflation communicated from abroad, or should it assume the risks connected with opposing that deflation by monetary expansion? The effects of the rapidly shrinking purchasing power of the exporter could have been lessened by the creation (on a sufficient scale) of purchasing power connected with the financing of temporary government deficits by borrowing the otherwise unused savings of individuals and by the expansion of bank credit. Among other things this would have tended to lower the value of the Canadian dollar in terms of foreign currency and thus to raise the Canadian dollar prices of goods sold abroad. This or some other type of monetary expansion and exchange depreciation, carried out with deftness and restraint, could have done much to prevent the drastic disequilibrium between the prices of primary products and costs and to avoid many of the gross inequities in the incidence of the depression. It is probable that the better balance between the incomes of different groups

and regions in the economy and between prices and costs brought about in this way, would have maintained the national income at a higher level and lessened the degree of unemployment. Because of the importance of fixed interest charges and the rigidity of wages (in both cases in Canadian currency) it would have been easier to resist the drop in exporters' prices (in Canadian dollars) than to force a reduction in their costs by allowing them to be fully exposed to external deflationary influences.

Early in the depression certain representatives of Western agriculture, seeking an escape from the pincers of falling prices and inflexible costs, urged upon the Dominion a policy of monetary expansion and currency depreciation. The proposals (the financing of public works with Dominion notes) were loosely formulated and suggested straight inflation. The Government was firmly opposed to such measures and announced its resolve to maintain adequate gold coverage for the currency.¹ The view that unbalanced budgets, financed by the expansion of bank credit and the issue of fiduciary currency, were desirable in certain contingencies, was regarded as rank heresy. The adoption of such measures was held as a sign of extreme weakness which should only be resorted to as a last effort to stave off complete collapse. The deliberate increase of purchasing power or the depreciation of the exchange in this manner, merely to counteract shrinking incomes from a temporary collapse of export prices or investment, was not regarded as a sufficient justification. This palliative was considered worse than the disease; it would shake confidence, harm public credit, impede the necessary readjustments, and hence merely delay recovery. These views of the Government faithfully reflected the most widely held opinions of businessmen, bankers and professional economists. The depreciation of the exchange, either directly or because of unorthodox monetary expansion, unless forced by extreme circumstances, was regarded as an act of "international immorality", carrying with it the stigma of default. For Canada, which was so heavily dependent on international trade and foreign credit, such action, it was thought, would be fraught with the most dire consequences. Canada, it was argued, should do nothing to weaken the confidence of either the internal or foreign investor; it should do everything in its power to keep the economy functioning without monetary manipula-

tion and thus facilitate the natural forces of readjustment and hasten the return of prosperity.

At the onset of the depression the Canadian foreign exchange position appeared to be extremely weak and the Canadian dollar seemed headed for depreciation. At the height of the boom the Government found it necessary to place restrictions upon the export of gold which was rapidly flowing out of the country. At the same time the foreign assets of the banks were being quickly depleted.² The principal factors in the pressure on the country's liquid reserves were the large outflows of capital connected with the extensive participation of Canadians in the New York stock market and the credit expansion of the banks who were able to maintain their cash reserves in spite of the loss of gold by borrowing Dominion notes under the Finance Act. But when the test came in 1930 the Canadian dollar did not depreciate. Canada, unlike other debtor countries, had not over-borrowed in the immediately preceding period; in fact she was a net capital exporter during all but the last year of the boom, and the economy was therefore not geared to a high rate of capital imports. In other debtor countries cessation of capital imports had had disastrous consequences and Canada was fortunate in not being vulnerable in this respect. In addition, Canada had an ample reserve of credit in New York which was a source of considerable strength. Much capital was required for the completion of projects initiated during the boom. The Dominion required funds for uncompleted transportation improvements, the provinces for public utilities and highways, the railways for branch lines, and private corporations for hydro-electric power developments, paper mills and mining projects. In 1930 Canada was able to sell abroad \$400 million of new securities, the greatest amount in its history, with the exception of 1913. During the same year, maturities of externally held debt which had averaged \$176 million annually since 1924, fell to \$110 million. With the collapse of the New York stock market boom the outflow of capital for the purchase of foreign securities virtually ceased. Consequently, net capital imports rose to \$315 million, nearly double those of 1929, and the highest since 1914. This large amount of foreign credits was more than enough to meet the deficiency in the exports of goods and services over the payments for imports and interest. There was thus no scarcity of foreign exchange and no reason for the Canadian dollar to depreciate. In fact, there was a surplus

¹ The country, however, had been technically off the gold standard since the end of 1928, when the Government placed unofficial restrictions on the free export of gold by the banks.

² During 1928 and 1929 the total of the exports of monetary gold and the sale of foreign assets of the banks amounted to \$136 million and \$125 million respectively.

of foreign funds available for the importation of \$36 million of monetary gold which greatly eased the cash position of the banks and enabled them to repay nearly all of their borrowings under the Finance Act.

The external position of Canada during 1930 was in sharp contrast to that of Australia and Argentina, its principal competitors in the export wheat market. The ability of both these countries to borrow abroad on long-term came to an abrupt end early in 1929. When in 1930 the value of their exports fell by one-third they were unable to muster,

held and by the end of January 1931, the Australian pound had depreciated to 23 per cent below its former gold parity.

Argentina departed from gold in December 1929, when the country's gold reserves were still very large.⁴ But the inelasticity of the currency system, the large amount of unfunded government obligations held by the banks, and continued government deficits made it extremely difficult to deflate the credit structure to the extent required for the maintenance of the gold standard. Furthermore, the repercussions of a very large fall in export prices

TABLE 51.—THE CANADIAN BALANCE OF PAYMENTS,^(a) 1928-34

(Millions of Dollars)

	1928	1929	1930	1931	1932	1933	1934
<i>Receipts and Payments for Commodities, Services, Interest and Dividends—</i>							
Receipts.....	1,880	1,728	1,374	1,047	888	838	1,040
Payments.....	1,804	1,961	1,624	1,156	912	823	961
Surplus (+) or Deficit (-).....	+ 76	-233	-250	-109	- 24	+ 15	+ 79
<i>Capital Movements—</i>							
New Canadian Securities Sold Abroad.....	207	297	400	200	104	134	111
Less: Retirements of Canadian Securities held Abroad.....	200	150	110	202	105	166	169
Net Sales (+) or Retirements (-).....	+ 7	+147	+290	- 2	- 1	- 32	- 58
Net Purchases (-) or Sales (+) by Canadians of Outstanding Securities held Abroad.....	-188	-105	- 13	- 24	- 16	+ 51	+ 9
Net Inflow (+) or Outflow (-) of Capital on account of Direct Investments, Insurance transactions, Government transactions, etc.	+ 12	+ 38	+ 38	+ 34	- 22	- 75	- 48
Net Sale (+) or Purchase (-) of Foreign Assets of Canadian Banks.....	+ 87	+ 88	-	+ 28	+ 28	+ 24	- 19
Total Net Capital Inflow (+) or Outflow (-).....	- 82	+168	+215	+ 36	- 11	- 32	- 116
Inflow (-) or Outflow (+) of Monetary Gold.....	+ 49	+ 37	- 36	+ 33	+ 3	+ 6	- 4
Errors and Omissions in the Estimates.....	- 43	+ 28	- 29	+ 40	+ 32	+ 11	+ 41
Total Amount of Foreign Exchange (+) or Canadian Dollars (-) required to pay for excess or deficit of imports of commodities, services, etc., over exports.....	- 76	+233	+250	+109	+ 24	- 15	- 79

^(a) Compiled from *The Canadian Balance of International Payments, 1928*, the Dominion Bureau of Statistics, Tables 49-51.

as Canada did, sufficient foreign exchange to fill the gap in their balances of payments. There was thus severe pressure on the exchanges. At first Australia tried energetically to prevent depreciation by restricting imports and by mobilizing its liquid reserves and using them freely for the maintenance of the currency at par. During 1930 Australia lost over \$100 million of gold and liquid foreign assets.³ Despite this large effort the exchange could not be

were extremely drastic because of the dependence of the solvency of the financial system on land values and the overwhelming importance of agricultural exports. It was economically impractical, as well as politically inexpedient, to impose the deflationary measures necessary for the maintenance of the exchange. Consequently, the Government permitted the peso to depreciate. Equilibrium in the balance of payments was thus achieved while,

³ "Through the whole of 1930 persistent efforts were made to keep the rate as near as possible to par with sterling." *Royal Commission on Monetary and Banking Systems, Commonwealth of Australia, 1937*, p. 68.

⁴ In December 1929, the Argentine gold reserve was equal to 77 per cent of the total outstanding currency. The amount of currency in circulation was relatively large since the bank cheque system was not highly developed.

at the same time, the money incomes of the exporters and the internal price structure were at least partially shielded against the sharp declines in external prices. The readjustments to the world depression were largely made by alterations in the relations between the Argentine and foreign currencies, rather than by alterations in the internal price and cost levels and the contraction of credit.⁵

The favourable factors which enabled the maintenance of equilibrium in the Canadian balance of payments with relative ease disappeared in 1931 as the world depression deepened. Capital imports virtually ceased, involving a decrease from the previous year of nearly \$300 million in available foreign exchange. Exports of commodities and services fell by nearly \$330 million. Yet the Canadian dollar did not depreciate until the British

deflationary influences and help to keep his prices more in line with his rigid costs. The Government, however, was stoutly opposed to any policy which would result in the depreciation of the currency because it feared (1) that it would be regarded as a form of international default and harm Canada's credit, and (2) that it would lead to inflation.

Although Canadian export prices fell drastically and the problems of readjustment to world deflationary forces were extremely difficult, the balance between the advantages and disadvantages of a policy of currency depreciation was at that time by no means clear. The Canadian balance of payments, in the total size of the transactions relative to the economy, in the number of unstable factors and in the close relations with each of the two most important international financial centres,

TABLE 52.—MONTHLY AVERAGE PRICES OF THE UNITED STATES DOLLAR AND THE POUND STERLING IN TERMS OF CANADIAN DOLLARS, 1930-34

	1930		1931		1932		1933		1934	
	\$ U.S.	£	\$ U.S.	£	\$ U.S.	£	\$ U.S.	£	\$ U.S.	£
January.....	1.01	4.92	1.00	4.86	1.17	4.03	1.14	3.85	1.00	5.07
February.....	1.01	4.89	1.00	4.86	1.15	3.96	1.20	4.10	1.01	5.08
March.....	1.00	4.87	1.00	4.85	1.12	4.06	1.20	4.13	1.00	5.11
April.....	1.00	4.86	1.00	4.86	1.11	4.17	1.18	4.23	1.00	5.15
May.....	1.00	4.87	1.00	4.86	1.13	4.16	1.14	4.50	1.00	5.10
June.....	1.00	4.86	1.00	4.88	1.15	4.21	1.11	4.61	.99	5.01
July.....	1.00	4.85	1.00	4.87	1.15	4.08	1.06	4.93	.99	4.99
August.....	1.00	4.86	1.00	4.87	1.14	3.97	1.06	4.79	.98	4.95
September.....	1.00	4.85	1.04	4.69	1.11	3.85	1.04	4.84	.97	4.86
October.....	1.00	4.85	1.12	4.38	1.10	3.72	1.02	4.79	.98	4.84
November.....	1.00	4.85	1.12	4.19	1.15	3.76	.99	5.08	.98	4.87
December.....	1.00	4.86	1.21	4.09	1.15	3.79	1.00	5.10	.99	4.89

abandonment of gold in September. The rapid decline in the national income, the curtailment of construction and the higher tariffs of 1930 and 1931 sharply reduced the purchases of foreign goods. The reduction in imports, however, was not sufficient to maintain the balance between the demand for foreign funds and the available supply. It was necessary to sell \$61 million of monetary gold and foreign banking assets.

In 1931 the continued fall in export prices and the increasing pressure from the depreciated currencies of Canada's principal competitors in the wheat market gave rise to an agitation in Parliament by independent Western members for the depreciation of the Canadian dollar. Such a policy, they argued, would relieve the farmer from external

is unlike that of any other country in the world. In addition to the highly fluctuating exports and capital imports, there was the unstable element arising out of the peculiar nature of Canada's external indebtedness. Over one-half of the total debt of all Canadian governments and over four-fifths of the bonded debt of Canadian corporations were either solely or optionally payable in a foreign currency.⁶ Because of their payment features, these obligations constitute a huge mass of international securities which readily flow back and forth across the boundaries, according to financial conditions in Canada, New York and London.⁷ The external obligations of other debtor nations are usually held by the foreign investors until they

⁵ The Argentine wholesale price level dropped remarkably little during the depression. Between 1929 and 1933 it fell but 10 per cent compared with about 30 per cent in Canada.

⁶ A large portion of these optionally payable securities, however, are held in Canada.

⁷ At times the gross amount of transactions in outstanding securities across Canada's border reaches a billion dollars a year.

mature and in the meantime are not likely to be sold back to the borrowing country. Whenever confidence in Canada's credit is seriously weakened, she may be confronted with large-scale dumping of securities into her market. Furthermore, the extensive United States branch-plant investments in Canada give rise to a considerable volume of liquid funds required as working capital or accumulated from profits which, under certain conditions, may be suddenly withdrawn. Normally the movements in the optional-pay securities and the branch plant balances are akin to the operations of a huge equalization fund which smooth out temporary or small scale fluctuations in the exchange. Under some circumstances, however, they constitute a serious danger since anything that causes foreigners to take an extremely pessimistic view of Canadian conditions may precipitate a large withdrawal of capital which might shatter the Canadian financial system and completely destroy Canadian credit, both internally and abroad. The effects on foreign confidence were, therefore, a main consideration in Canadian monetary and exchange policy during the depression. The Federal Government, confronted with the early maturity of hundreds of millions of optional-pay public securities and facing the necessity of financing increasing deficits was inclined to be cautious. Furthermore, any measures leading to the depreciation of the exchange would add to the cost of interest charges and thus heap increased burdens on governments already harassed by falling revenues. Many private corporations, selling mainly in the domestic market, had no means of financing higher debt charges and would have been forced into bankruptcy.⁹

The risks attached to a policy of exchange depreciation or monetary expansion were magnified in the minds of the Government by the absence of any reliable machinery. Lacking a central bank or some other established institution it would not be possible, it was thought, to carry out such a policy in a manner which would command the confidence of either the Canadian or foreign financial community. The proposals to issue fiduciary currency or simply to buy foreign exchange in some undefined way smacked of pure inflation. While these methods would have brought about depreciation of the exchange, the Government was not certain that it could keep either inflation or depreciation within control. In any case, the Government felt that inflation in whatever form

or for whatever purpose was neither a cure nor a palliative for the ills of the country.⁹

Because of the dangers and uncertainties which the Government thought were involved in any aggressive monetary measures to combat the deflation, it stuck resolutely to "sound" and orthodox policies. When Britain abandoned the gold standard in September, 1931, it simply allowed the Canadian dollar to find its own level.¹⁰ Thereafter, until the United States devaluation in 1933, the Canadian dollar moved roughly half-way between the United States dollar and sterling with an average discount below the former during 1932 of about 13 per cent and a premium over the latter of 22 per cent. The unpredictable course of sterling, together with the considerations already discussed, restrained the Government from linking the dollar to the pound despite the disadvantages suffered by exporters to the United Kingdom. Having important relations with each of the two principal monetary centres, Canada followed the lead of neither. The position of exporters would have been improved by tying the dollar to sterling but debt charges in the United States would have risen.

After October, 1932, some positive measures were taken to promote easy money and the groundwork was begun for the establishment of a central bank by means of which, among other things, such a policy could be methodically carried out.¹¹ The Dominion sought to refund as much of its obligations as possible at lower interest rates which, besides reducing the cost of the debt service, tended to lower the whole structure of interest rates. In November, 1932, and again in June, 1934, the Government endeavoured to expand bank cash

⁹ "Much has been heard in recent months about inflation. Some of the advantages claimed for inflation may seem alluring to industries harassed by falling prices and declining turnover. But let the sponsors of inflation never forget that apart from the other difficulties and dangers involved in their program, one inevitable result would be a fight from our dollar, a withdrawal on a large scale of the capital invested by foreigners in this country in the form of securities and bank deposits. There are also to be considered internal reactions to any steps which might impair confidence in a country's currency. Against policies which might lead to such dangers, this government has resolutely set its face." Hon. E. N. Rhodes, Minister of Finance, *Budget Speech*, March 21, 1933, p. 8.

¹⁰ "There are some who advocate that our dollar should be tied to sterling at the old parity and still others who criticize what they mistakenly believe to be a policy of pegging our dollar in terms of New York. This is not the time to enter into a discussion of this broad and complicated question. Suffice it for me to say that our dollar has been allowed to find its own level and that as a result it has been fluctuating about half-way between the United States dollar and the English pound. In so doing it may be working out a not unsatisfactory compromise between those of our national interests which would be benefited by close and stable relations with sterling, and those on the other hand which would be seriously harmed by a heavy and fluctuating discount in terms of New York." Hon. E. N. Rhodes, Minister of Finance, *Budget Speech*, March 21, 1933, p. 8.

¹¹ For a more detailed treatment of the Government's efforts to promote easy money after 1932 and of other phases of Canadian monetary policy during the depression, see F. A. Knox, *Domestic Monetary Policy (1929-34)*. (Manuscript.)

⁹ Higher debt charges arising out of currency depreciation were not a serious problem in the case of Argentina. Less than one-fifth of the total external debt of Argentina was payable in a foreign currency.

by the issue of \$35 million and \$52.5 million respectively of Dominion notes. The former had involved an equal amount of borrowing under the Finance Act and was not very effective. The latter issue which was used to finance expenditures on public works added substantially to the cash reserves of the banks. By that time, however, the worst had passed. Export prices were rising; the United States had devalued and the Canadian dollar was again at par with sterling. The easy money policy was then very largely a matter of keeping in step with rising business activity and with the easy money policies of the United States and Great Britain.

In view of the possible dangers connected with deliberate currency depreciation, which so greatly influenced the attitude of the Government, it is important to make a general, even if non-quantitative estimate, of the probable gains which exporters would have derived from such a policy. The two main exports, wheat and newsprint, were in the weakest position to benefit. Large surplus stocks and the import restrictions of European countries were unfavourable factors in the case of wheat. Furthermore, the Government's activities in the wheat market introduced an arbitrary and unpredictable element. It is conceivable that depreciation would simply have reduced the Liverpool sterling price by an equal proportion, thus eliminating any improvement in the dollar receipts. However, marketing policies could have been adopted which would have retained a large portion of the benefits of depreciation for the Canadian producer. If the Government had undertaken to depreciate the exchange for the purpose of assisting the exporters, it is reasonable to expect that it would have adapted its marketing policy in accordance with that objective. In any case, the disadvantages of the Canadian producer in competition with the depreciated currencies of Australia^{11*} and Argentina would have been reduced.

Newsprint was in a particularly precarious situation. Over-capacity, high fixed charges, and competitive conditions made it extremely unlikely that the producers of this commodity would have benefited from the lower value of the Canadian dollar.

There was a wide range of products, however, whose internal prices would have been improved

by the depreciation of the exchange to the level of sterling. Gold, base metals, fish, meat and dairy products, live stock, lumber and exports of manufactures were all in the position to retain the whole or some of the higher Canadian dollar values of foreign currencies. This group of goods constituted about one-half of the total exports. Better prices for these commodities would have been an important influence in reducing the disparities in the incidence of the depression. The immensely important tourist trade would also have benefited considerably as American tourists would have been attracted by the premium on their dollars. It is improbable that the beneficial effects of a better balance between prices and costs in important industries and regions of the country would have been completely offset by the higher costs of imports and increased debt charges. If the increases in the prices of imports were an important limiting factor they could have been compensated for to a considerable extent by a reduction of tariffs without lowering the level of protection previously enjoyed. It is true that the main industry of the most seriously affected region, the Prairie Provinces, would perhaps have gained very little. However, many of their minor products, such as live stock and dairy products, would have benefited and in any case they could hardly have suffered from more favourable conditions in the other exporting areas of the country.

The monetary and exchange policies which were followed rendered the disparities in the incidence of the depression greater than they needed to have been. The decline in the national income was also probably greater. The risks and dangers connected with monetary expansion and currency depreciation were great and a mistaken or careless procedure would undoubtedly have brought the consequences which the Government feared. But a skilful policy, which perhaps was not too much to expect in view of the serious problems of the time, could have avoided them. It would have been possible by any one of a number, or by a combination, of methods, such as restricting the outflow of gold, restraining the contraction of credit, avoiding an increase of protective tariffs, and purchasing foreign exchange, to depress the exchange value of the dollar without causing a wild flight of capital or a serious loss of foreign confidence in Canadian credit. The lack of a central bank or other ready-made machinery was not an insuperable obstacle. A suitable organization could have been readily set up as was done in other countries far less favourably situated.

^{11*}The Australians who appeared before me in London regarded the abandonment of the gold standard early in the depression as having operated to the benefit of the exporting producers more than anything else." *Report of the Royal Grain Inquiry Commission, 1938, p. 132. See also Royal Commission on Wheat Flour and Broad Industries, Second Report, (Australia), 1934-35.*

Prior to September, 1931, a policy of currency devaluation was impractical in view of the nature of public opinion and the attitude of the financial community. With the British abandonment of gold, however, the dollar could have been depreciated, directly with sterling or independently, without producing a serious shock to confidence. Had such a course been followed, Canada would have been at least partially shielded against the deflationary influences arising out of the discount on the monetary unit of one of her principal markets. She would also have been spared increased exchange disadvantages in competition with the important group of countries whose currencies fell with the pound.

Tariff Policy—sharp tariff increases and other import restrictions to maintain employment in manufacturing intensified cost rigidities of primary producers and enhanced burden of depression falling on exporters

A positive depression policy of the Federal Government was the attempt to maintain employment in Canadian manufacturing industries by increasing restrictions on imports. The Government announced as a principle that it was unsound to import goods which were or could be produced in Canada as long as Canadian labour and equipment were unemployed.¹¹⁵ It argued that a reduction of purchases from abroad would also produce a

TABLE 53.—TARIFF CHANGES, 1928-36

	Year	Equivalent <i>Ad Valorem</i> Tariff Rates ^(a) (Unweighted Averages)			Ratio of Imports to Gross Value of Production ^(b)			
		Preferential	Treaty	General	Preferential	Treaty ^(c)	General ^(c)	Total
All Manufactures.....	1928	12	17	21	4	2	20	25
	1933	14	25	30	4	1	8	13
	1936	10	24	30	4	6	4	14
All Textiles.....	1928	17	23	28	18	7	13	39
	1933	21	39	45	10	2	4	17
	1936	20	41	49	11	4	2	16
All Iron and Steel Products.....	1928	11	17	19	3	1	51	54
	1933	10	23	25	8	1	24	33
	1936	6	21	25	5	21	8	34
Electrical Apparatus and Supplies.....	1928	15	23	27	2	—	29	32
	1933	16	30	34	2	—	15	17
	1936	12	29	33	2	14	2	18
Glass and its Products.....	1928	13	19	22	9	16	47	72
	1933	12	23	26	11	7	38	56
	1936	7	20	25	13	38	16	67
Petroleum Products.....	1928	9	12	14	—	—	33	23
	1933	10	15	21	—	—	13	13
	1936	7	16	18	—	8	4	12
Leather Boots and Shoes.....	1928	16	27	29	2	—	4	6
	1933	24	37	43	1	—	1	2
	1936	20	37	43	1	2	—	3
Furniture.....	1928	18	28	30	—	—	—	—
	1933	22	32	49	—	—	—	—
	1936	18	31	49	—	—	—	—

^(a) Unweighted arithmetical averages of *ad valorem* rates and *ad valorem* equivalents of specific rates on each tariff item of manufactured goods imported calculated from duties collected and customs valuations. Since the necessary information was not available dumping duties were not included and no adjustments were made for arbitrary over-valuations. The averages, therefore, tend to understate the tariff increases between 1928 and 1933. See, W. A. Mackintosh, *The Economic Background of Dominion-Provincial Relations*, pp. 90-94.

^(b) The value of Canadian production is "gross," i.e., includes cost of materials purchased and the value of imports includes commodities in various stages of manufacture. Hence the absolute size of the ratio of imports to gross value of production does not necessarily measure the relative importance of imports and domestic production. However, changes in the ratio from one year to another do show the changes in the volume of imports in relation to home production. All that is intended here is to show such changes between 1928, 1933 and 1936.

^(c) Note that, after the United States Trade Agreement of 1934, the Treaty, and not the General Tariff as previously, applied to most of the non-preferential trade.

¹¹⁵ " . . . every import brought into this country, from abroad, represents foreign trade to some other country. Our business is to see that we do not expand the foreign trade of any other country when we ourselves are producing or can produce the goods so imported." Minister of Finance, *Budget Speech*, June 1, 1931, p. 45.

favourable balance of payments, prevent the depreciation of the exchange, and thus help to maintain Canada's credit. Accordingly, during 1930-32 the tariff was sharply raised. Every major secondary industry¹² was granted higher duties and Canada changed from a country of moderate to one of high protection. The averages of the General and Intermediate rates (which applied to over four-fifths of the total imports) on all manufactured goods were raised by nearly 50 per cent. All the important commodities of general consumption were made subject to substantially increased duties. The average of the rates on textiles rose by about one-fourth in the Preferential schedule and by two-thirds in the Intermediate and General. Wool and artificial silk duties were approximately doubled. Tariffs on boots and shoes, furniture, and petroleum products were boosted by about one-half. Virtually every branch of the iron and steel industry received added protection by an increase in duties in the Intermediate and General schedules of approximately one-third.

The raising of tariffs, however, was but one phase of the Government's efforts to reduce imports. During 1930-33 administrative restrictions were greatly intensified. Devices for the exclusion of goods which the regular tariff did not keep out were multiplied and made more effective. The Minister responsible for the administration of customs was given sweeping powers to levy special dumping duties on the basis of arbitrary valuations. The Minister, among other things, was empowered to fix for duty purposes, the value of any imports which, in his opinion, were harmful to Canadian producers. Prior to the Trade Agreement with the United States in 1935, arbitrary valuations were regularly applied to such important items as textile fabrics, rubber footwear, wearing apparel, fruits and vegetables, automobiles, and electrical apparatus which, in many cases, raised the real rates of protection to fantastic heights.¹³ In addition to arbitrary valuations the Government also used its power to fix arbitrarily the exchange rate for duty purposes of any foreign currency which had depreciated. Thus, when sterling went off gold, its value for the purpose of

calculating the duty on imports from Britain was fixed considerably above the actual rate.¹⁴

Higher tariffs, administrative restrictions and the increasing weight of specific duties on falling prices, were effective in causing a considerable diversion of demands from foreign to domestic producers. Whereas in 1928 the value of imports of all manufactured goods was equal to 25 per cent of the total gross value of Canadian manufacturing production, by 1933 this ratio had fallen to 13 per cent. The reduction of imports relative to home production was particularly pronounced in the case of textiles, automobiles, electrical apparatus, gasoline, furniture, implements, and machinery—all of which are important items either in the cost of living or the cost of production of primary producers. Employment in the protected manufacturing industry was better maintained than in other branches of goods production (except mining). The decline in salaries and wages paid by the former was appreciably less than the fall in the national income.^{14*}

Efforts to check the fall in employment by reduction of imports were helpful mainly to the manufacturing areas of Central Canada and to the coal and iron industries of Nova Scotia. In so far as the relative improvement of incomes in these places was due to the maintenance of prices resulting from higher tariffs, they were harmful to the rest of the country.

For upwards of 40 years there had been no substantial change in the general level of tariff protection. The settlement and development of the Prairie Provinces and British Columbia had been begun and carried to an advanced stage of maturity under approximately the same tariff conditions. Industries, governments and homes had been established with the tariff as one of the given factors, like the climate and the natural resources. It is true that the tariff limited the extent of the development and the rise in the value of the natural resources but it did not deprive either individuals or governments of opportunities and incomes which they had ever actually enjoyed. Nor did it, under conditions of expansion and high mobility, reduce the earnings of capital and labour below what they would have obtained elsewhere in Canada.¹⁵

¹² "The rates in our tariff schedules were made having in mind parity of exchange. Consequently when the pound sterling became depreciated, it was necessary to value it for purposes of special or dumping duty at \$4.40, in order to offset in part the advantage which the British exporter obtained in our markets as a result of the depreciated pound." Hon. E. N. Rhodes, Minister of Finance, *Budget Speech*, March 21, 1933, p. 23.

¹³ See Table 49, p. 150.

¹⁴ For a more complete exposition of the nature of tariff "burdens" and the relation of the tariff to Canadian economic development, see W. A. Mackintosh, *The Economic Background of Dominion-Provincial Relations*, Chap. VII.

¹² The duties on many agricultural commodities were also raised but in most instances they could have no effect, since for nearly all of these items Canada was on an export basis.

¹³ See *Report of the Royal Commission on the Textile Industry*, 1938, pp. 13-16.

In the case of the Maritime Provinces, however, the effects were different. The Maritime economy had reached a mature development before the National Policy tariff was adopted. Its introduction (1879) constituted a drastic change in the conditions under which the population and its economic activities had grown up. The higher duties suddenly increased the costs of production of the important export industries. This reduced net incomes and the value of property in these industries below what was already established or what they would otherwise have been. The failure of the Maritimes to expand economically and to prosper to the same extent as the rest of Canada was due to more basic circumstances but the tariff was an important contributing factor. It hastened the decline of the old export industries and retarded the growth of the new. Since many of the local resources were of a marginal character, the restrictions of the tariff to their development for export was a serious disadvantage. The rise of the Nova Scotia coal and iron industries was almost entirely dependent upon protection and bounties but this expansion was not sufficient to offset the losses suffered in other Maritime industries.

Prior to 1930 the protective tariff was not a "burden" on Western Canada in the sense that it lowered earnings of capital and labour below those received in the rest of Canada or reduced the value of investments previously made. The sharp increases of duties and administrative restrictions during 1930-32, however, were entirely different in this respect. The rise in tariffs and the maintenance of the prices of manufactured goods which this permitted brought a relative increase in costs and greatly worsened the conditions under which exporting industries were operating—and this at a time when the prices of their products were falling drastically. The share of exporters in the national income was reduced below what it otherwise would have been, the decline in the value of their property was intensified, and the burden of their debts was increased. The only way in which exporters could adjust themselves to the fall in the prices in foreign markets was by reducing their costs. Since the cost of living and the prices of manufactured goods were everywhere more rigid than the prices of raw materials, costs would have fallen more slowly than exporters' receipts even if the tariff had remained unchanged. The raising of tariffs greatly worsened a situation which already was highly unfavourable. As a result the standards of living were further reduced and the defaults of debt became more general.

The increase in protection widened the domestic market for the Canadian producer and thus helped to maintain employment and income in the manufacturing industry. But had tariffs not been raised the purchasing power of exporters would have been greater, debt defaults would have been less and the expansion of such industries as gold mining and electric power would have been more rapid. It is possible that these circumstances would have contributed just as much to the maintenance of the market for Canadian manufacturers as did the rise in duties, and that the national income would have remained at a higher level. While no definite

TABLE 54.—COST TO PURCHASERS OF TARIFF PROTECTED MANUFACTURED GOODS^(a) IN TERMS OF EXPORT COMMODITIES

1929 = 100

	All Export Prices	Wheat	Lumber	Live-stock	Fish	Non-Ferrous Metals
1929.....	100	100	100	100	100	100
1930.....	111	132	107	104	103	114
1931.....	124	201	118	144	123	135
1932.....	145	206	130	176	142	145
1933.....	143	189	125	192	143	133

^(a) Includes all manufactured textiles, boots and shoes, pottery, glass and its products, chemicals and allied products, cement, gasoline, and all manufactures of iron and steel.

conclusion can be reached on this point, one thing is clear; the increased restrictions to imports added considerably to the wide disparities in the incidence of the depression on the various industries and regions.

Some of the disabilities of exporting industries under the higher tariffs were reduced by the Empire Trade Agreements in 1932. The British preferences on lumber, apples, and bacon were valuable. The former two were important to British Columbia and the Maritimes but the agricultural industries in the Prairies got little help. Because of surplus Empire production, the 6 cent preference on wheat was of no assistance. Moreover, the reduction in Canadian duties was not significant in lowering the costs of production of exporting industries generally. Further relief did not come until the Trade Agreement with the United States in 1935. Under this Agreement valuable concessions were obtained for lumber, cattle, fresh and frozen fish, whiskey, and potatoes. The general reduction in tariffs against United States goods, special reductions in the case of farm implements, certain classes of automobiles, electrical apparatus, gasoline, many kinds of machinery, and abolition

of arbitrary valuations on a large list of items were important. However, the average level of the Canadian tariff remained far above that existing prior to 1930.

4. PUBLIC FINANCE, 1930-37

Severe Strain of Unequal Incidence of the Depression on the Decentralized System of Canadian Public Finance—large inter-regional transfers of income by Federal Government

Perhaps the outstanding feature of the great depression in Canada was the enormous strain which was placed on the public finance system. The severity of this strain was closely related to the nature of the economy, the constitutional division of powers and responsibilities, and the economic policies of the Dominion. It must be emphasized at the outset that the nature of the economy made it inevitable that serious public finance problems would have to be faced, whatever economic policies were adopted. The slump in export prices and the consequent worsening in the terms of trade with other countries, the increase in the heavy burden of external debts, and the collapse of investment, made it impossible to escape a sharp reduction in the real national income. The manner in which this reduction was distributed over the various regions, industries, classes and occupational groups was nevertheless highly significant, especially in a federal state. When a country is divided up into a number of parts with distinct economic characteristics, each with separate and independent political authorities responsible for costly government services within their respective areas, the incidence of a decline in the total income is immensely important. If the distribution of the decline is fairly uniform each separate governmental unit could perhaps carry the increasing burdens without great difficulty. If the losses fall very disproportionately upon certain regions, the public finances of some areas may be carried on with relative ease, while others are likely to break down with serious repercussions upon the financial, economic and constitutional structure of the entire country.

It is clear from the review in section 2 of this chapter that the disparities in the impact of the depression on various regions and provinces were extremely great. The controls over the tariffs and monetary conditions were powerful instruments in the hands of the Federal Government for the modification of the unequal incidence. However, the national economic policies which were adopted,

whether or not they were wise in view of all the circumstances, did little to improve this situation and in some respects intensified it. In so far as these policies were not used to bring about a more even distribution of losses, the greater was the strain on the decentralized system of Canadian public finance. The larger the decline in the income and the larger the consequent rise in government expenditures in the most unfavourably situated provinces, the more rapidly did local revenues and credit become hopelessly inadequate and the larger was the support which had to be obtained from the Dominion.

The nature and course of the depression in Canada inevitably involved large inter-regional and inter-governmental transfers of income by the Federal Government. These transfers took several forms—assistance to a few severely depressed industries, assistance to all provincial governments to help in financing costs of relief, and special assistance to the most hard-pressed provincial governments to prevent defaults of debt and enable continuation of essential services.

Federal Assistance to Industry—the heavy burden of the overhead costs of the National Railways; assistance to wheat and coal

The most important federal transfers to industry consisted of the payment of the deficit of the Canadian National Railways, the cost of the intervention in the wheat market, and the payment of transportation and other subventions to the coal industry. There were few activities which were more severely affected by the depression and the technical changes of the thirties than that of railway transportation. The Canadian railways, besides being built on a scale which involved a highly optimistic estimate of the future of the country, were heavily dependent upon the large investment and developmental expenditures which expansion to such a future would entail. The factors responsible for the collapse of investment brought both a sharp reduction of revenues and an increase in the burden of carrying over-extended facilities. The drought in Western Canada and the slump in wheat prices struck at the heart of the Canadian railway structure. The design of the transcontinental lines through all-Canadian territory was dependent upon the mid-continental location and the prosperity of the country's principal exporting region. When crop failures and large unsold surpluses reduced the amount of bulk freight to be hauled out and sharply curtailed the more remunerative back-haul of manufactured goods, the

full burden of the tremendous overhead of long connecting lines of railway through unproductive territory was felt. While the drop in investment, the fall in wheat prices and the drought brought a drastic reduction to long-haul bulk traffic in both directions, motor truck competition was rapidly cutting into the profitable high class, short-haul traffic in Ontario and Quebec. Under this combination of unfavourable circumstances railway revenues fell by more than 50 per cent between 1928 and 1933. Over the same period the deficit of the Canadian National Railways, which had to be met by the Federal Government, rose by over \$60 million (including interest on government investment and advances), a figure twice as great as the Dominion's share of all relief costs in the latter year.

Railways were unable to bolster their falling revenues by an increase in freight rates and it would have been undesirable, from the point of view of the national income, to do so. In fact, there is a strong argument that certain rates ought to have been reduced as part of the Dominion's economic policies to soften the impact of the depression on exposed groups. However, even with railway freight rates substantially unchanged, the burden falling on the taxpayers rose rapidly. During 1932-34 the Dominion paid nearly 40 per cent of the total transportation costs of all the freight hauled by the Canadian National Railways. This load on the taxpayer was perhaps more in the nature of a transfer to investors than it was a transfer to the users of railway facilities. In the case of the Canadian Pacific Railway and the privately-owned railways of other countries, the depression losses fell mainly upon the owners of railway securities. Such a shifting of losses is not possible under government ownership. Canada had in part forsaken the flexibility of private ownership in favour of government guarantees and government ownership in order to build an economically integrated and united nation and to stimulate nation-wide expansion. These purposes, together with past mistakes, converted an enormous transportation overhead into the inescapable fixed charges of government. This was one of the more important of the many rigidities which so greatly enhanced the difficulties of readjustment to the world depression.

The plight of Western agriculture was quickly recognized. The Federal Government, whose economic policies did little to soften the impact of the depression on the wheat farmer, undertook to alleviate his position by means of public finance.

When wheat prices began to fall precipitously in the autumn of 1930, the Dominion guaranteed the initial payment set by the Pools and a General Manager of the Central Selling Agency having the confidence of the Government was appointed to take charge of the carry-over and to market the 1930 crop. In the following year the contract pools were terminated and the initial payment or minimum price system was abandoned. In that year (1931) the Federal Government paid a bonus of five cents per bushel on all wheat marketed.

TABLE 55—EXPENDITURES ON TRANSPORTATION BY THE DOMINION—CURRENT ACCOUNT, 1928-37

(Thousands of Dollars)

	Canadian National Railway Deficit ^(a)	Harbours Steamships and Marine	Canals and other Transportation	Total Transportation	Percentage of Total Current Revenues of the Dominion
					%
1928.....	47,788	9,627	15,295	72,710	16.2
1929.....	64,457	11,574	17,554	93,615	21.7
1930.....	85,542	11,044	20,191	117,777	34.1
1931.....	112,196	10,237	14,747	137,170	42.3
1932.....	112,807	8,531	10,277	131,715	44.1
1933.....	109,234	8,419	9,327	126,980	40.6
1934.....	91,160	9,222	10,780	111,162	31.8
1935.....	92,414	10,292	11,960	114,636	31.7
1936.....	71,898	9,115	11,528	92,541	29.9
1937.....	67,635	9,584	11,468	88,687	17.7

^(a) Includes interest on government investment and advances.

The bonus was discontinued in 1932 and instead a "stabilization" policy was begun. Throughout the period, 1932 to September, 1935, the Government, through the General Manager of the Central Selling Agency, made large purchases of futures on the Winnipeg Exchange for the purpose of maintaining or raising the open market price at which farmers sold their wheat. While these efforts at times held the Canadian wheat price above comparative world prices, they did not, however, prevent it from falling to disastrously low levels. The attempt to "stabilize" the value of Canada's principal export sold on a shrinking world market was a bold venture. The unsold stocks which accumulated and were held by the Government assumed large proportions and involved an increasingly hazardous risk to the taxpayer. When the Wheat Board was established in the autumn of 1935 and the "stabilization" operations came to an end, the Government had on hand some 205 million bushels of wheat. However, the continuation of the drought in North America, a short crop in the Argentine, and world economic recovery brought a sharp rise in prices during the following year and the Wheat Board was able to sell the whole

of the carry-over in a relatively short period with a small net profit to the Government. The minimum prices set by the Board for the 1935 and 1936 crops resulted in losses of about \$12 million.

Although the Government's wheat marketing policy during the depression entailed considerable risks, the total cost to the taxpayer proved in the end to be relatively small—a total of about \$20 million (including the five cent bonus) during 1930-37, or less than an average of one cent per bushel over the period. The drastic impact of the depression on Prairie agriculture was not significantly reduced by government assistance.

collapse of investment, the falling markets for exports and the contraction of manufacturing had to be looked after in other ways. Canada had never experienced an unemployment problem of such magnitude. During previous periods of economic depression the problems of unemployment and destitution had usually found their solution in the self-sufficiency of the household, in the solidarity of the family, in the establishment of new homes on the agricultural frontier, in the decline of immigration, and in the increase of emigration to the United States. By 1930 such opportunities for self-reliance and methods of adjustment had all

TABLE 56.—TOTAL RELIEF AND OTHER PUBLIC WELFARE EXPENDITURES
(Millions of Dollars)

	Relief ^(a)	Old Age Pensions	Other Public Welfare				Total Relief and Other Public Welfare	Percent of National Income
			Dom.	Prov. ^(b)	Mun.	Total		
								%
1928.....	—	1.9	6.2	21.3	24.5	52.0	53.9	1.2
1929.....	—	3.5	6.7	22.8	26.4	55.9	59.4	1.3
1930.....	18.4	11.8	7.6	24.4	28.3	60.3	90.5	2.2
1931.....	96.5	16.2	6.4	24.7	28.5	59.6	172.3	4.9
1932.....	95.0	16.4	5.6	24.7	28.0	58.9	170.3	6.0
1933.....	97.9	16.7	5.4	23.6	28.9	58.1	172.7	6.6
1934.....	158.5	20.0	5.3	26.5	30.8	62.6	241.1	8.4
1935.....	172.9	22.8	6.2	26.5	32.7	65.4	281.1	8.4
1936.....	160.3	29.6	6.6	28.5	35.4	70.5	260.4	7.6
1937.....	165.1	38.9	6.8	34.8	35.6	77.2	281.2	7.3

^(a) Includes all expenditures on relief, i.e., agricultural, public works, direct and miscellaneous.

^(b) Less refunds from municipalities.

The financial help received by the coal industry from the Federal Government was important. The transportation subventions for the movement of Canadian coal to Central Canada were started in 1928 but they did not have much effect until the thirties. These subventions together with the bonuses to Canadian coal used for coking, which were begun during 1930-32, became a considerable factor in the provision of markets. In 1936 the total subsidies received by the coal mines in Nova Scotia amounted to about 15 per cent of the total wages paid by the industry.

Federal Assistance to Provinces—municipal-provincial revenues hopelessly inadequate to finance the whole cost of relief

The problems arising out of the wide disparities in the incidence of the depression were dealt with to only a minor extent by the federal transfers to industry. The destitute wheat farmers, the wage-earners who were thrown out of work by the

but disappeared. The livelihood of hundreds of thousands of citizens seemed to be entirely dependent upon public charity. The cost had to be met through large transfers of income from the employed to the unemployed and from one region to another by means of taxation and government borrowings.

The constitutional responsibility for unemployment relief rested with the provinces. The municipalities, however, were generally regarded as primarily responsible since up until this depression it had been seldom necessary to recognize the distinction between cyclical mass unemployment and "poor relief". The conditions which arose after 1930 soon demonstrated that provincial and municipal responsibility could not be rigorously insisted on in practice. The relief problem related broadly to two quite different situations—the prairie wheat farmers stricken by drought and ruinous prices, and the unemployed wage-earners who tended to concentrate in large urban centres and in single-industry towns. It became clear that neither of these situa-

tions could be dealt with on the basis of local responsibility. The municipalities in the drought area which had lost the whole of their income could not maintain existing essential services, much less pay out large sums to meet the operating costs of the farms. Real estate values in many urban centres would have collapsed completely under the taxation and debts necessary to take care of the local concentrations of unemployed. However, even if the relief burden had been uniformly distributed over all the municipalities of the country it would have been necessary to increase tax collections from real estate by 50 per cent. This was quite impossible.

assistance of the Dominion with its powers of taxation and borrowing was essential. When the problem became acute in 1930 the Dominion began the temporary arrangements for extending financial help to the provinces which were continued throughout the depression. The constitutional responsibility of the provinces (and their municipalities) was still adhered to in form. The Dominion undertook merely to assist the former because of the "extraordinary conditions" and because the problem had "become so general . . . as to constitute a matter of national concern". Administration and initiation of relief projects remained the responsibility of the provinces and

TABLE 57.—THE BURDEN OF RELIEF ON THE PROVINCES AND THE MUNICIPALITIES 1930-37

(Millions of Dollars)

	1930	1931	1932	1933	1934	1935	1936	1937
Total Mun.-Prov. Current Revenues.....	492	479	480	479	484	508	530	558
Total Mun.-Prov. Current Expenditures ^(a) excluding Relief.....	491	492	490	479	462	485	483	514
Surplus available for Relief or Deficit.....	1	13	10	—	2	23	47	44
Total Relief Costs Expended through Mun.-Prov. Agencies.....	17	92	92	90	141	134	134	152
Deficiency of Mun.-Prov. Revenues.....	16	105	102	90	139	111	87	100
Less Share of Relief Assumed by Dominion.....	3	34	34	28	43	41	52	55
Mun.-Prov. Deficit.....	13	71	68	62	96	70	35	53

^(a) Including municipal sinking fund contributions and debt retirement.

The relief costs could only be met with the wider revenue and credit sources of the senior governments. The resources of the provincial governments, however, were not by themselves sufficient. Over the whole period 1931-37 the relief expenditures amounted to more than 25 per cent of the total municipal-provincial revenues. In nearly every province during the early thirties these revenues fell short of the requirements for ordinary purposes. There were distressing deficits even before anything had been provided for relief. In not one province in any year following 1930 did the municipal-provincial revenues left over after provision for ordinary services meet the total cost of relief. The amount of borrowings necessary to pay for the whole of the remaining requirements would have bankrupted most of the provinces and municipalities in the country.

The magnitude of relief costs hopelessly exceeded the financial capacities of the provinces and the municipalities. During the eight-year period their combined revenues fell short of total relief and current expenditures by over \$750 million. The

municipalities. Aside from its own public works programs and relief for unemployed single transients, the Dominion simply gave grants-in-aid to help finance the expenditures of other governments. In this manner the federal authority assumed about 40 per cent of the total outlays on relief during the 1930-37 period. In addition it loaned \$106 million to the four Western Provinces to enable them to meet their portions of the cost.

The problem of financing sharply rising outlays for relief would have been difficult enough had the costs fallen evenly upon the various sections of the country. The extreme differences which occurred, however, greatly aggravated the situation. The wide disparities and the regional incidence of the depression had, as a consequence, large variations in the incidence of the burden of relief and other welfare costs upon the several provinces.

The costs of relief varied inversely with the ability to meet them. In Western Canada, where incomes fell most rapidly, relief costs were relatively the highest. The weight of the burden in Saskatchewan, the Province most severely

affected, was about five times as great as that in the Maritimes and Ontario, the Provinces least affected. Total relief expenditures during the eight-year period amounted to nearly two-thirds of the total municipal-provincial revenues in Saskatchewan compared with about one-fifth in the Maritimes and Ontario. A burden with such extreme variations in its incidence could not be

region to another. The greater the disparities in the incidence of the depression and the greater the failure to use national economic policies to reduce these disparities, the larger were the transfers which had to be made.

We shall now examine the financial situation which developed in each of the provinces.

Prince Edward Island

Relief expenditures in Prince Edward Island, the most rural province in Canada, were relatively small. There were no large industries or urban concentrations in which mass unemployment could arise. The self-sufficiency of the farm household and the farm family was still an important feature of the economy. Consequently per capita costs for relief of unemployment were the lowest in Canada. Over four-fifths of the expenditures incurred for this purpose were devoted to public works instead of direct relief. This outlay was more of an effort to use idle labour for the provision of community facilities rather than an unavoidable expense for the relief of destitution. While the total expenditures were small compared with those of the rest of Canada, they nevertheless weighed heavily upon the finances of the Province which had no large incomes nor large accumulations of wealth. Virtually the whole of the provincial-municipal share of the relief costs were borrowed, and this added nearly 50 per cent to governmental debts during the period, 1930-37. This increase in the deadweight load placed a considerable strain on the meagre revenue sources.

TABLE 58.—DISPARITIES IN THE BURDEN OF RELIEF ON THE VARIOUS PROVINCES, 1930-37

	Ratios of Total Relief Costs to Total Provincial Incomes	
	Relative Severity of Burden—Index of Ratios—National average = 100	Percentages ^(a)
Saskatchewan.....	367	15.3
Manitoba.....	115	4.2
British Columbia.....	100	3.6
Alberta.....	100	3.6
All Provinces—National Average.....	100	3.6
Quebec.....	90	3.2
Prince Edward Island.....	76	2.8
Ontario.....	78	2.7
Nova Scotia.....	70	2.6
New Brunswick.....	67	2.4

^(a) Percentage of total relief expenditures in the province to total provincial income.

entirely carried with local resources. The Dominion not only had to come to the aid of all the provinces, but it had to help some provinces more than others. It was necessary to use the national powers of taxation and borrowing to transfer income from one

TABLE 59.—PRINCE EDWARD ISLAND—THE COST OF RELIEF AND MUNICIPAL-PROVINCIAL FINANCES, 1930-37

(Millions of Dollars)

	1930	1931	1932	1933	1934	1935	1936	1937
Total Mun.-Prov. Current Revenues.....	1.58	1.56	1.63	1.64	1.67	1.79	1.95	2.06
Total Mun.-Prov. Current Expenditures ^(a) excluding Relief.....	1.55	1.79	1.58	1.61	1.76	1.97	1.76	1.92
Surplus available for Relief or Deficit.....	.03	.23	.05	.03	.09	.18	.19	.14
Total Relief Costs expended through Mun.-Prov. Agencies.....	.03	.32	.24	.06	.41	.94	.62	.58
Deficiency of Mun.-Prov. Revenues.....	—	.55	.19	.03	.50	1.12	.43	.44
Less Share of Relief Assumed by Dominion.....	.02	.18	.05	.02	.22	.29	.32	.18
Mun.-Prov. Deficit or Surplus.....	.02	.37	.14	.01	.28	.83	.11	.26

^(a) Including municipal sinking fund contributions and debt retirement.

Nova Scotia

Although the prices of Nova Scotia's exports fell drastically the burden of relief was relatively small. The nature of the economy prevented the widespread destitution which appeared in other parts of Canada. The exporting industries were composed largely of small-scale individual enterprisers, namely, fishermen, farmers, and lumbermen, who retained a relatively high degree of self-sufficiency. When their prices dropped their standards of living had to be sharply reduced but they were not entirely without food and shelter. Aside from the coal and steel industries there were no large industrial concentrations. Tariff increases and Dominion trans-

total expenditures by all governments on direct relief. The latter added only \$2 million to the provincial debt, but highways added over \$30 million. The Province took advantage of its high credit standing, low interest rates and idle labour to provide facilities which it hoped would stimulate economic development. Whether or not the highways will turn out to be a significant factor in helping to overcome some of the long-run economic difficulties of the area, they have greatly intensified the problems of provincial government finance. The limited revenue sources of the Province cannot easily carry the heavy fixed charges of large dead-weight debts.

TABLE 60—NOVA SCOTIA—THE COST OF RELIEF AND MUNICIPAL-PROVINCIAL FINANCES, 1930-37

(Millions of Dollars)

	1930	1931	1932	1933	1934	1935	1936	1937
Total Mun.-Prov. Current Revenues.....	15.2	16.0	15.7	14.9	15.9	18.2	18.7	19.3
Total Mun.-Prov. Current Expenditures ^a excluding Relief.....	15.0	15.7	15.5	16.0	16.6	18.6	17.3	18.2
Surplus available for Relief or Deficit.....	.2	.3	.2	1.1	.7	.3	1.4	1.1
Total Relief Costs expended through Mun.-Prov. Agencies....	.1	2.6	3.8	3.2	2.4	3.0	2.7	2.6
Deficiency or Surplus of Mun.-Prov. Revenues.....	.1	2.3	3.6	4.5	3.1	3.3	1.3	2.5
Less Share of Relief Assumed by Dominion.....	.1	.9	1.4	1.1	.8	1.2	1.3	.7
Mun.-Prov. Deficit or Surplus.....	.2	1.4	2.2	3.2	2.3	2.0	—	.8
Capital Expenditures on Highways not included in Relief	1.9	1.3	.5	1.8	2.1	4.4	5.5	7.8

^a Including municipal sinking fund contributions and debt retirement.

portation subventions to coal helped considerably to maintain employment in the steel mills and the coal mines. Hence no severe or protracted problem of mass unemployment arose. However, there were many on the farms and in the towns who, in one way or another, obtained a livelihood but could not find satisfactory jobs, and there were many who lived on the margin of subsistence. Emigration which had been an important outlet in former years was greatly reduced. There were not sufficient opportunities for the growing population. Thus in Nova Scotia the main problem was to find permanent means for employment rather than to relieve a temporary situation. The provincial government undertook a large-scale program of highway construction with the object of providing both immediate employment and of expanding the capacity of the economy by encouraging the tourist trade and reducing the costs of transportation. During the eight-year period 1930-37 capital outlay on highways was nearly four times as great as the

New Brunswick

The situation in New Brunswick was similar to that in Nova Scotia. The forest and agricultural industries which dominated the economy of New Brunswick afforded considerable scope for alternative employment and self-sufficiency. The sale of pulpwood to the pulp and paper mills which continued to operate at a high rate of capacity throughout the depression provided a source of income to many farmers and labourers. The British preferences granted in the Empire Trade Agreements brought a considerable revival in lumber production after 1933. Prices of farm products and the earnings that could be obtained from working in the woods were tragically low but for nearly everyone it was possible to get the means of subsistence which greatly reduced the extent of government relief. The most important development in provincial finance during the depression in New Brunswick as in Nova Scotia was the large capital outlays on highways. However, the scale of the

TABLE 61.—NEW BRUNSWICK—THE COST OF RELIEF AND MUNICIPAL-PROVINCIAL FINANCES, 1930-37

(Millions of Dollars)

	1930	1931	1932	1933	1934	1935	1936	1937
Total Mun.-Prov. Current Revenues.....	12.0	11.7	11.3	11.0	11.4	12.1	12.8	14.1
Total Mun.-Prov. Current Expenditures ^(a) excluding Relief.....	12.0	11.4	11.3	11.2	11.4	12.1	12.3	12.9
Surplus available for Relief or Deficit.....	—	.3	—	.2	—	—	.5	1.3
Total Relief Costs expended through Mun.-Prov. Agencies.....	.3	2.6	.5	1.9	1.3	2.4	2.5	1.5
Deficiency of Mun.-Prov. Revenues.....	.3	2.3	.5	2.1	1.3	2.4	2.0	.3
Less Share of Relief Assumed by Dominion.....	.3	.7	.4	.6	.4	1.1	.9	.6
Mun.-Prov. Deficit or Surplus.....	—	1.6	.1	1.5	.9	1.3	1.1	.3
Capital Expenditures on Highways not included in Relief	6.6	2.3	1.6	.3	.7	3.9	3.1	9.1

^(a) Including municipal sinking fund contributions and debt retirement.

expenditures relative to the economy was considerably greater. Consequently the finances of the Province got into an even more vulnerable position. In 1937 the accumulated per capita outstanding debt incurred for highways in New Brunswick was one-third higher than in any other province. During that year net debt charges, about nine-tenths of which were due to highways, absorbed 37 per cent of the total current revenues of the Province.

Quebec

Relief in Quebec was very largely concerned with the problem of mass unemployment in the metropolitan area of Montreal. This area, the largest urban concentration in the country, contains nearly 40 per cent of the population of the Province and is very closely dependent upon Western Canada. Montreal, with its railway termini, shipping, manufactures, financial and distributive facilities, constitutes the entrepôt to

the great exporting industries of the West which are the bases of the transcontinental economy. The sharp drop in the purchasing power of that exporting region reacted directly and severely upon Montreal. The destitution which arose from the resulting unemployment could only be relieved with government assistance. In such a large industrial concentration there were few opportunities for self-sufficiency or alternative employments. The burden upon both municipal and industrial finances was great. The assistance from the Dominion took care of less than 30 per cent of the costs. The portions left to the local governments far exceeded the amounts that could feasibly be raised by provincial or municipal taxes and virtually the whole of the requirements were borrowed. The total relief capitalized by the Provincial Government during 1930-1938 was almost equal to the total outstanding debt of the Province at the beginning of the period. Relief was largely responsible for the rise in the municipal debt of

TABLE 62.—QUEBEC—THE COST OF RELIEF AND MUNICIPAL-PROVINCIAL FINANCES, 1930-37

(Millions of Dollars)

	1930	1931	1932	1933	1934	1935	1936	1937
Total Mun.-Prov. Current Revenues.....	115.0	111.2	110.4	110.2	116.5	123.4	126.7	141.8
Total Mun.-Prov. Current Expenditures ^(a) excluding Relief.....	110.5	110.8	115.8	115.8	117.2	125.5	127.2	136.7
Surplus available for Relief or Deficit.....	4.5	.4	5.4	5.6	.7	2.1	.5	5.1
Total Relief Costs expended through Mun.-Prov. Agencies.....	2.0	17.3	18.8	22.2	31.8	26.5	35.4	30.8
Deficiency or Surplus of Mun.-Prov. Revenues.....	2.5	15.9	24.2	27.8	32.5	28.6	35.9	25.7
Less Share of Relief Assumed by Dominion.....	.3	5.1	5.8	4.7	11.3	7.9	10.4	8.0
Mun.-Prov. Deficit or Surplus.....	2.8	11.8	18.4	23.1	21.2	20.7	25.5	17.7

^(a) Including municipal sinking fund contributions and debt retirement.

metropolitan Montreal from \$252 million to \$345 million between 1930 and 1937. The Quebec municipalities were required to assume a considerably larger share of the total relief expenditures than municipalities elsewhere in Canada (28 per cent in Quebec compared with 15 per cent in all the rest of Canada). Consequently, the municipal finances of Quebec, especially of Montreal, emerged from the depression in a far more weakened condition than was the case in other parts of the country.

Over 70 per cent of the total outlay for unemployment was for direct relief. At the beginning and at the end of the period large expenditures were made on public works. These, however, proved to be extremely costly in comparison with other methods of dealing with the relief of distress. In certain circumstances it may be most economical in the long run to choose a time of idle resources to construct needed capital facilities, but desirable results cannot be obtained without careful planning, adequate financial resources and control of monetary affairs. The experience of Quebec along with that of other provinces demonstrated that the municipal-provincial revenue systems cannot support the huge expenditures which are involved in dealing with prolonged unemployment by means of public works.

While the sums which were spent on what was formally classified as relief reached large proportions, they did not include all the outlays for this purpose. The aid given by the Church, which had long fulfilled an important role in providing social services in Quebec, greatly reduced the costs which fell on governments. Furthermore, the Provincial Government undertook a number of activities which were not regarded as relief but whose main object nevertheless was to alleviate distress and provide

employment. Between 1930 and 1937 the Province spent \$26 million on colonization of settlers, \$54 million on highway construction, and \$14 million on loans to farmers. These activities, whether or not they were necessary or wise, were all more or less closely associated with the depression. Together with expenditures for relief, they brought a three-fold increase in the provincial debt, a rise more rapid than that in any other province. Between 1930 and 1937 the per capita municipal-provincial deadweight debt rose from one of the lowest to one of the highest in the country.

Ontario

Unemployment in Ontario was largely the result of the contraction of manufacturing output and the collapse of the investment boom of the late twenties. The condition was most serious in industries which were directly dependent upon the markets of Western Canada and in the construction trades. While the situation was severe in certain industrial areas, such as Windsor and Toronto, and in a number of one-industry towns, the problem of meeting the costs of relief for the Province as a whole was not nearly as difficult as that in other parts of Canada. The total relief expenditures amounted to 19 per cent of the municipal-provincial revenues of the period compared with 27 per cent for the remainder of the Dominion. Ontario, in which were concentrated the greater part of the country's large individual and corporate incomes and wealth, had relatively easy access to additional government revenue. The Province also was the centre of gold mining, the nation's most rapidly developing industry, which both directly and indirectly provided many opportunities for employment and new sources of government income. Total municipal-provincial revenues

TABLE 63.—ONTARIO—THE COST OF RELIEF AND MUNICIPAL-PROVINCIAL FINANCES, 1930-37

(Millions of Dollars)

	1930	1931	1932	1933	1934	1935	1936	1937
Total Mun.-Prov. Current Revenues.....	189.2	188.3	187.8	188.6	185.9	198.3	212.5	216.1
Total Mun.-Prov. Current Expenditures ^(a) excluding Relief.....	188.8	189.2	189.3	182.4	185.9	179.0	179.6	195.4
Surplus available for Relief or Deficit.....	.4	.9	1.5	6.2	—	19.3	32.9	20.7
Total Relief Costs expended through Mun.-Prov. Agencies.....	2.4	21.3	33.4	32.4	60.7	54.5	38.5	28.2
Deficiency of Mun.-Prov. Revenues.....	2.0	22.2	34.9	26.2	60.7	35.2	5.6	7.5
Less Share of Relief Assumed by Dominion.....	1.2	9.4	9.5	11.9	15.5	15.5	15.1	7.4
Mun.-Prov. Deficit or Surplus.....	.8	12.8	25.4	14.3	45.2	19.7	9.5	.1

^(a) Including municipal sinking fund contributions and debt retirement.

fell but slightly between 1930 and 1934, and rose considerably thereafter. After 1934 the Province and its municipalities were able to meet a substantial portion of their share of relief costs out of current receipts. The amount per capita of relief capitalized in Ontario was the lowest of any province in the Dominion with the exception of the Maritimes. The outstanding municipal-provincial debt rose by 18 per cent compared with 40 per cent in the rest of the country. Although the burden of relief brought a number of municipalities into default, the total municipal debt of Ontario declined by 13 per cent during the period.

Ontario spent a much larger proportion of her total relief outlay (36 per cent) on public works than did any of the other provinces with the exception of the Maritimes. This was partly due to the rapid development of the northern areas which provided better opportunities for useful works than appeared elsewhere. However, it was also a reflection of the relatively greater revenue and credit resources of this Province.

Manitoba

The burden of relief in Manitoba was more severe than in any other province except Saskatchewan. Eighty to 90 per cent of the total costs were incurred in the metropolitan area of Winnipeg. The depressed conditions in that centre were associated

and the great wheat-growing area to the West which lies mainly beyond the boundaries of the Province. When the volume of that commerce was drastically curtailed by ruinous farm prices and a succession of unprecedented droughts in Saskatchewan the economic support of nearly 40 per cent of Manitoba's population virtually collapsed. The problem of unemployment was intensified by the accumulation of idle workers from the whole Prairie area. Winnipeg normally contains a large pool of labour from which many of the seasonal workers needed on the wheat lands are recruited. When jobs disappeared the labourers remained on the relief rolls of the city. Winnipeg was, therefore, required to take care of a substantial share of the misfortunes of the large industrial reserve army of the wheat-growing industry for whose condition the city was in no way responsible.

There was no surplus of municipal-provincial revenues with which to meet the sharply rising expenditures for relief. Between 1931 and 1933 the Province imposed sharp increases in taxation, including a wage tax which raised the provincial tax structure to the highest level in Canada. However, the receipts from the new and additional imposts did no more than make up for the declines in municipal-provincial revenues from previous sources. The greater portion of the outlays on relief had to be borrowed. By 1932 the credit of the Province

TABLE 64.—MANITOBA—THE COST OF RELIEF AND MUNICIPAL-PROVINCIAL FINANCES, 1930-37

(Millions of Dollars)

	1930	1931	1932	1933	1934	1935	1936	1937
Total Mun.-Prov. Current Revenues.....	34.5	32.8	33.7	35.1	34.7	34.1	34.3	35.4
Total Mun.-Prov. Current Expenditures ^(a) excluding Relief.....	34.3	34.7	35.9	34.6	32.8	32.1	31.1	31.4
Surplus available for Relief or Deficit.....	.2	1.9	2.2	.5	1.9	2.0	3.2	4.0
Total Relief Costs expended through Mun.-Prov. Agencies.....	1.6	8.6	7.4	7.1	7.5	9.8	12.2	9.8
Deficiency of Mun.-Prov. Revenues.....	1.4	10.5	9.6	6.6	5.6	7.8	9.0	5.8
Less Share of Relief Assumed by Dominion.....	.3	3.3	2.8	2.5	2.2	3.3	5.1	3.5
Mun.-Prov. Deficit.....	1.1	7.2	6.8	4.1	3.4	4.5	3.9	2.3
Dominion Loans to the Province for Relief, and General Purposes ^(b)	—	2.9	1.6	1.2	4.4	4.2	4.9	2.7

^(a) Including municipal sinking fund contributions and debt retirement.

^(b) \$805,000 of these advances were written off by the Dominion in 1937.

only in a small way with circumstances within Manitoba itself. The drought was a minor factor and agriculture is of far less relative importance than in the other two Prairie Provinces. The prosperity of Winnipeg is very directly dependent upon the vast flow of commerce between the East

and its municipalities was exhausted. Most of the suburban municipalities around Winnipeg had defaulted on their debts. Thereafter the money for capitalized relief and current deficits could only be obtained by means of provincial loans from the Dominion. The Province in turn made loans to

municipalities. For several years, also, the maturing obligations of the Province were refunded with Dominion advances. At the end of 1937 the indebtedness to the Federal Government was \$22 million, or nearly one-fifth of the total outstanding provincial debt. In addition, the Dominion had guaranteed provincial bank loans amounting to \$12 million. The municipalities owed the Province \$4 million.

Saskatchewan

Canada's most serious economic troubles during the thirties had their origin in the impact of the world depression and drought upon the wheat-growing industry of Saskatchewan. This industry, upon which the interdependence and economic integration of the country were chiefly based, suffered the most unfavourable coincidence of circumstances

averaged less than one-half that of the decade of the twenties. Such a decline, in the face of the high fixed costs of Western agriculture, would have caused general and drastic hardship. The addition of the drought brought outright and widespread destitution, as well as complete inability to operate farms without government assistance.

The area affected by successive crop failures was about equal to one-quarter of the total improved farm acreage of Canada. It contained nearly one-half the rural inhabitants of Saskatchewan. In 1931, one-half; in 1933-4-6, one-third; and in 1937, two-thirds of the total farm population of the Province was destitute. Not only was this large section of the population dependent for livelihood upon public charity, but the operating expenses of from one-third to two-thirds of Canada's largest export industry had to be met by the Gov-

TABLE 65.—SASKATCHEWAN—THE COST OF RELIEF AND MUNICIPAL-PROVINCIAL FINANCES, 1930-37

(Millions of Dollars)

	1930	1931	1932	1933	1934	1935	1936	1937
Total Mun.-Prov. Current Revenues.....	41.5	37.9	39.4	38.7	36.5	36.8	35.4	38.3
Total Mun.-Prov. Current Expenditures ^(a) excluding Relief....	43.0	41.0	39.4	38.5	38.1	37.6	35.7	36.7
Surplus available for Relief or Deficit.....	1.5	3.1	—	.2	1.6	.8	.3	1.6
Total Relief Costs expended through Mun.-Prov. Agencies.....	5.9	24.0	13.2	10.3	21.1	18.6	22.7	62.3
Deficiency of Mun.-Prov. Revenues.....	7.4	27.1	13.2	10.1	22.7	19.4	23.0	60.7
Less Share of Relief assumed by Dominion.....	.5	7.9	7.1	2.4	8.0	7.2	11.3	27.5
Mun.-Prov. Deficit.....	6.9	19.2	6.1	7.7	14.7	12.2	11.7	33.2
Dominion Loans to Province for Relief and General Purposes ^(b)	—	11.5	5.3	8.1	13.5	11.1	6.1	11.5
Seed Grain Bank Loans Guaranteed by Dominion.....	—	—	—	—	—	—	2.6	14.5

^(a) Including municipal sinking fund contributions and debt retirement.

^(b) \$17.7 million of these advances were written off by the Dominion in 1937.

in its history. If the repercussions upon other sections of the Dominion were widespread and severe, the conditions in Saskatchewan were nothing short of disastrous. Economically this area was the most vulnerable in Canada. No other province was so completely dependent upon the fluctuations in the export market. Nowhere was production so dependent upon the vagaries of the climate.

Ruinous prices and drought were about equally responsible for the disaster. The forces which so intensified the world depression fell with particular severity on wheat. The national economic policies of the Dominion did virtually nothing to soften the blow. The full exposure to the adverse world influences drove the prices received by the farmer to levels which during the period 1930-35

erment. It was the latter which chiefly distinguished Saskatchewan's problem from that in the other provinces. In the other provinces it was mainly a matter of providing food, fuel, clothing and shelter for unemployed wage-earners. In the case of the Saskatchewan wheat farmer the failure of a crop involved not merely the loss of the means of livelihood but also the working capital invested in that crop. This working capital had to be made available before there was another chance of the farmer becoming self-supporting. The provision year after year of seed, feed, fodder and supplies to tens of thousands of large-scale farmers entailed a huge financial burden not encountered in the relief of industrial unemployment. The per capita costs in Saskatchewan for agricultural aid alone (seed,

feed, etc.) was greater than the total per capita disbursements for all relief purposes in the other provinces.

The costs of direct and agricultural relief completely overwhelmed the finances of the Province and its municipalities. These costs during 1930-37 never fell to less than 27 per cent (1933) of the total municipal-provincial revenues, and in 1937 they rose to 163 per cent of such revenues. For the whole period the relief expenditures amounted to 60 per cent (compared with 21 per cent for the rest of the country) of the total ordinary receipts of the Province and its municipalities combined. Although new taxes were imposed and rates increased, revenues could not be maintained at levels required to provide adequate ordinary government services, much less to pay for any part of relief costs. It was manifestly impossible to meet any significant portion of the outlay on relief by means of local taxation when total expenditures for this purpose for the eight-year period exceeded the total net farm cash income of the whole Province.

TABLE 66.—RELIEF EXPENDITURES IN SASKATCHEWAN AND THE REST OF CANADA

	Total Relief Expenditures 1930-37	
	Saskatchewan	Other Canada
Percentage of Total Income.....	13.6	3.1
Percentage of Municipal— Provincial Current Revenues....	60.5	20.1
Per Capita (dollars).....	196	76

During 1929 and 1930 there were severe droughts in the central and south central sections of the Province. The greater portion of the cost for agricultural aid fell on the municipalities who borrowed the money by means of provincially guaranteed bank loans. In 1931, when the crop failure was even more widespread, the municipalities were at the end of their tether. The Provincial Government was not in a much better position. For three decades the expansion of Saskatchewan's wheat industry had been a major factor in the prosperity, in the growth of large incomes and in the accumulation of wealth in some of the older regions of Canada. The Province had no access either by taxation or borrowing to this surplus, which its industry had created during prosperity, to tide it over the years of adversity. Such a transfer of income, which was absolutely essential to prevent widespread starvation and the

collapse of the wheat industry, could only be brought about by means of national taxation and the borrowing powers of the Dominion. After 1930 the Dominion assumed substantial portions of the total relief expenditure. For several years the Federal Government paid 100 per cent of the cost of rural relief and agricultural aid in the drought area. However, the share of the burden left with the Province proved to be far in excess of its credit resources. After 1932 its borrowing powers were gone. Henceforth the Dominion provided nearly the whole of the funds required for relief either by direct payment of the cost or by loans directly to the Province or by guarantees to the banks. The share of relief disbursements assumed by the Federal Government in Saskatchewan was larger than that in any other province, viz., one-half, compared with one-third in the rest of the country. Direct and guaranteed Dominion loans supplied 35 per cent of the total outlay. Only about 15 per cent of the funds required for relief were raised by the Province and the municipalities. Nevertheless the share (50 per cent) of the burden left as the responsibility of the provincial and municipal governments involved the addition of large amounts to the provincial debt. The portion which the municipalities as a whole were able to assume was less than 5 per cent of the total cost (that is after write-offs and subsequent adjustments). The Provincial Government undertook, either directly or indirectly, virtually the whole of the liability in excess of the Dominion share. Between 1930 and 1937 the total debt of the Provincial Government was more than doubled. Three-quarters of this increase was due to relief. In 1929 the per capita deadweight debt of the Province of Saskatchewan was the lowest in Canada with the exception of Quebec; in 1937 it was the highest.

Alberta

The severity of the relief burden in Alberta was approximately equal to that of the average for all provinces. On a per capita basis the outlay was the lowest in Canada with the exception of the Maritimes and Quebec. Total expenditures for unemployment and agricultural aid in Alberta amounted to only slightly more than one-fourth of that in Saskatchewan and three-fourths of that in Manitoba. While there were a number of crop failures in some sections of the Province, the total area affected was relatively small. The average yield per acre of wheat during 1930-37 was only slightly below normal and exceeded that of Saskatchewan by nearly 60 per cent. Furthermore, irrigation in the southwest and a considerable

degree of mixed farming elsewhere made Alberta's agriculture more self-sufficient than that of her wheat-growing neighbour to the east. The total cost for agricultural aid in Alberta for the eight-year period amounted to \$6.4 million, or less than one-fifth of the cost in Saskatchewan for the single year of 1937.

The incidence of ruinously low prices, however, was perhaps more severe than elsewhere. Owing to the more recent development of Alberta fixed debt charges were relatively higher than in any other province. In addition, farmers had not had time to become as well established. Under these circumstances, the drastic fall in prices of agricultural products produced a relatively greater strain on the farming industry and on governments. Alberta's depression problem was more one of debt and high overhead costs than one of widespread destitution.

However, despite large expenditures, the relief burden did not intensify the municipal debt problem. Over the period, Alberta municipalities as a whole were able to reduce their total outstanding debts by over 20 per cent, a percentage reduction greater than in any other province. This, however, was only accomplished with a heavy burden of taxation on falling real estate values.

During the first half of the period the share of relief assumed by the Provincial Government was entirely financed out of borrowings. After 1932, Alberta, like other Western Provinces, could no longer borrow on her own credit. Thereafter, the Dominion supplied the necessary loans. After 1934 the imposition of new taxes, increases in rates together with a measure of recovery produced a rise in revenues, but the Province remained unable to meet the full costs of its portion of relief. However, following the arbitrary reduction of debt

TABLE 67.—ALBERTA—THE COST OF RELIEF AND MUNICIPAL-PROVINCIAL FINANCES, 1930-37

(Millions of Dollars)

	1930	1931	1932	1933	1934	1935	1936	1937
Total Mun.-Prov. Current Revenues.....	36.6	34.4	35.5	35.2	36.1	36.3	38.7	39.2
Total Mun.-Prov. Current Expenditures ^(a) excluding Relief.....	38.0	39.4	36.7	35.6	35.2	35.1	33.2	33.2
Surplus available for Relief, or Deficit.....	1.4	5.0	1.2	.4	.9	1.2	5.5	6.0
Total Relief Costs expended through Mun.-Prov. Agencies.....	2.4	6.7	5.9	4.9	6.0	7.0	9.2	7.6
Deficiency of Mun.-Prov. Revenues.....	3.8	11.7	7.1	5.3	5.1	5.8	3.7	1.6
Less Share of Relief Assumed by Dominion.....	.2	2.6	2.6	1.5	1.6	1.8	3.6	3.7
Mun.-Prov. Deficit or Surplus.....	3.6	9.1	4.5	3.8	3.5	4.8	.1	2.1
Dominion Loans to Province for Relief and General Purposes..	—	1.0	1.9	2.1	3.9	7.7	.8	2.2

^(a) Including municipal sinking fund contributions and debt retirement.

Alberta's relief expenditures arose very largely out of the unemployment which prevailed in the cities, principally Calgary and Edmonton. These cities were mainly dependent on the distribution of goods and supplies to the farms, and upon investment resulting from rapid settlement of the frontier. When low prices and heavy fixed costs sharply curtailed farm purchasing power and reduced agricultural expansion, opportunities for employment declined. Furthermore, these centres became havens of refuge for workers and farmers who had left the land. Alberta municipalities were required to assume a slightly larger share of total relief costs than in other parts of Canada. Since their ability to borrow quickly disappeared, the whole of the funds had to be raised by taxation and by loans from the Provincial Government.

charges by one-half in 1936, the Province was able to finance without further borrowings. Between 1930 and 1937 the provincial debt rose by \$32 million, over 50 per cent of which was due to relief. This represented a rate of increase less than half as rapid as that which took place on the average in other provinces. Alberta's per capita deadweight debt, however, was one of the highest in Canada.

British Columbia

The British Columbia economy was fully exposed to the unfavourable influences of the world depression. Employment was heavily dependent upon production for foreign markets. As the prices and markets for raw material exports fell, unemployment became chronic. Unlike the Maritimes or the Prairie Provinces, British Columbia's export

industries are operated by large-scale corporate methods in which the workers are wholly dependent upon wages. In the former Provinces, where individual enterprise located in rural areas is predominant, at least some degree of self-sufficiency is possible. In British Columbia, when export markets and prices decline sharply, large numbers of labourers are left completely without means of support and must be looked after by public relief.

municipalities were tided over by the provincial assumption of a larger portion of the total costs of relief and by provincial loans. During the last two years British Columbia municipalities were required to contribute less than 9 per cent of the total outlay. This easing of the burden by the Province avoided dangerous increases in the municipal debt which would otherwise have been necessary.

TABLE 68.—BRITISH COLUMBIA—THE COST OF RELIEF AND MUNICIPAL-PROVINCIAL FINANCES, 1930-37

(Millions of Dollars)

	1930	1931	1932	1933	1934	1935	1936	1937
Total Mun.-Prov. Current Revenues.....	46.8	45.4	44.1	44.0	45.8	47.4	48.6	52.1
Total Mun.-Prov. Current Expenditures ^(a) excluding Relief....	47.5	47.7	44.8	43.2	43.0	43.3	44.4	47.6
Surplus available for Relief or Deficit.....	.7	2.3	.7	.8	2.8	4.1	4.2	4.5
Total Relief Costs expended through Mun.-Prov. Agencies....	2.2	8.4	8.9	8.1	9.9	11.3	10.0	9.0
Deficiency of Mun.-Prov. Revenues.....	2.9	10.7	9.6	7.3	7.1	7.2	5.8	4.5
Less Share of Relief Assumed by Dominion.....	.3	3.4	4.1	3.4	3.2	2.3	3.5	3.1
Mun.-Prov. Deficit.....	2.6	7.3	5.5	3.9	3.9	4.9	2.3	1.4
Dominion Loans to Province for Relief and General Purposes...	—	1.6	2.2	1.9	4.0	6.6	4.0	2.9

^(a) Including municipal sinking fund contributions and debt retirement.

Prior to the depression British Columbia was the most rapidly growing province in Canada, and a relatively larger number of workers than elsewhere were drawn into the construction industry. When the investment boom collapsed the unemployment problem on this account was relatively more severe. The difficulties were enhanced by the fact that most of the expansion took place in the metropolitan area of Vancouver which contains nearly half the population of British Columbia. This concentration of the population in one urban centre was greater than that in any other province. The relief problem was further intensified by the migration of many unemployed labourers from the Prairie Provinces to the milder climate of the coast city.

As a consequence of these various factors, per capita relief expenditures in British Columbia were the largest in Canada with the exception of Saskatchewan. Relative to the provincial income, however, they were less burdensome than in any of the Prairie Provinces. During the first half of the period none of the relief costs were met out of current revenues. Debts rose rapidly and by 1933 the credit of the Province and the municipalities was exhausted. Henceforth the necessary loans had to be obtained from the Dominion. The

After 1933 higher taxes and improvement in export prices produced a sharp rise in provincial revenues. In 1937 these revenues were almost 30 per cent higher than they were in 1930. In each of the years 1934 and 1937 substantial portions of the relief expenditures were met out of current receipts. Thus, in spite of a continuing heavy relief burden, increases in provincial debt were held at a relatively low level. Between 1930 and 1937 total liabilities rose 35 per cent compared with 57 per cent for all provincial governments. British Columbia's per capita deadweight debt, however, was for many years the highest in Canada. In 1937 it was only slightly below that of Saskatchewan.

Results of Dominion Insistence on Primary Prov.-Mun. Responsibility for Relief—large Dom. expenditures without adequate control, large deficit spending with wasteful results, creation of unwieldy prov. and mun. debts, virtual breakdown of finances of several provinces

It is clear from the above brief review that there was no co-ordinated or carefully planned relief policy in Canada during the depression. It was a policy of expediency which failed either to promote

maximum welfare under the circumstances or to safeguard the financial position of the various governments. The Dominion, from whom alone leadership could have come, was mainly concerned with steering a day-to-day course between insisting on the constitutional responsibility of the provinces and the necessity of preventing widespread starvation. Although the Dominion provided nearly one-half of the total funds, and over 70 per cent in the case of the Western Provinces, it did not have adequate control over the money which was spent and administered by nine different provinces and by hundreds of municipalities, each trying to get along as best it could without much thought of the others. Because of limited financial resources and dependence upon the Dominion no province could carry out an efficient and economic program of its own. The grant-in-aid policy of the Federal Government, which involved an expenditure of federal money amounting to \$162 per capita in Saskatchewan and only \$23 to \$12 per capita in the Eastern Provinces, resulted in large transfers of income from one section of the country to another under conditions that gave no assurance that the transfers were spent in a manner which produced the greatest national benefits. Because of the wide disparities in the incidence of the depression and the effects of the national economic policies large transfers were inevitable, but their basic purpose should have been to enhance the national welfare. As it turned out, glaring and unjustifiable differences in relief standards arose;¹ large amounts of federal money were either directly or indirectly loaned to farmers and municipalities without proper safeguards as to repayment; free movement of labour to jobs was impeded by a maze of local relief regulations; many homeless unemployed were pushed from pillar to post; and large sums were wasted by conflicting and offsetting policies which were followed in different parts of the country.

Although a large amount of federal funds was spent the conditions under which the money was given did not prevent breakdowns in municipal-provincial finance. The grant-in-aid policy was based on the premise that the province (with its municipalities) was constitutionally responsible and that it should, therefore, carry as much of the burden of relief within its area as possible. The province in turn tended to hold the municipalities responsible and to push the financial burden as far as possible on their shoulders. As a consequence

nearly all the provinces and many municipalities were drawn to the edge of financial solvency and some were pushed over and became bankrupt. Some municipalities and governments of every province, with the possible exception of the two Central Provinces, acquired heavy deadweight relief debts which their limited taxing powers cannot carry indefinitely. The Western Provinces either temporarily or permanently lost their financial independence and could only continue to function with Dominion loans and in some cases with partial default of debt charges. In 1937, one-fifth of the total municipal-provincial revenues were absorbed by the interest on non-self-supporting debts.

TABLE 69.—DOMINION RELIEF EXPENDITURES IN EACH OF THE PROVINCES THROUGH MUNICIPAL-PROVINCIAL AGENCIES, PER CAPITA AND PORTION OF TOTAL FUNDS PROVIDED, 1930-37

	Per Capita (dollars)			Percentage of Total Funds Provided by Dominion
	Dom. Share	Dom. Loans	Total	
				%
Prince Edward Island.....	14	—	14	40
Nova Scotia.....	14	—	14	37
New Brunswick.....	12	—	12	29
Quebec.....	17	—	17	29
Ontario.....	23	—	23	52
Manitoba.....	33	29	62	69
Saskatchewan.....	96	66	162	85
Alberta.....	33	23	56	71
British Columbia.....	31	31	62	66
TOTAL.....	36		37	44

Deficit spending occurred on a large scale, but because of the unrelated policies of numerous governments, it did not produce, assuming it was necessary and desirable, the most efficient results. Some provinces spent large amounts on public works while others drastically curtailed such outlays. Some endeavoured strenuously to minimize the increases in debt to preserve their credit while others borrowed extensively with consequent harm to the credit of their more cautious neighbours as well as to their own; some fulfilled their portions of national projects while others could not, or would not, do so. Had the relief deficits been centralized in the one authority which had control of monetary policy and possessed the national powers of taxation, the money could have been obtained at considerably lower interest rates and could have been spent effectively as part of a general and co-ordinated employment and recovery program. In the latter case the country could have emerged from the depression with government finance as a

¹ See Appendix 6.—A. E. Grauer, *Public Assistance and Social Insurance*, pp. 22-28. See also this Report, Book II, Sect. A, Ch. 1 for further discussion of this problem and for recommendations thereon.

TABLE 70.—THE EFFECT OF RELIEF ON MUNICIPAL-PROVINCIAL DEBTS—1930-1937

(Millions of Dollars)

	Prince Edward Island	Nova Scotia	New Brunsw- wick	Que- bec	On- tario	Man- itoba	Sas- katche- wan	Al- berta	British Col- umbia	TOTAL
Outstanding Debt 1930.....	4.4	79.0	69.4	458.7	1,064.3	202.9	163.7	204.5	237.5	2,484.4
Total capitalized Relief and Current De- ficits.....	2.0	11.9	6.2	138.4	108.0	31.4	87.1	22.9	29.2	437.1
Other Capital Expenditures and Advances Net.....	3.0	29.4	28.9	211.8	189.4	14.6	30.0	2.5	28.5	508.9
Less Contributions to Municipal Sinking Funds and Debt Retirement.....	.9	3.5	2.2	49.1	106.7	10.2	7.2	8.8	10.5	199.0
Outstanding Debt 1937.....	8.5	116.8	102.4	759.8	1,255.0	209.5	273.6	221.1	284.7	3,231.4
Percentage of Debt Charges to Current Revenues, 1937.....	16	20	27	21	17	21	23	15 ^(a)	21	19

^(a) At reduced rates.

whole in a much stronger position, the virtual breakdown of provincial finance could have been avoided and there could have been much more to show for the debts both in terms of human welfare and in material productive equipment. The decentralization of the deficits made it extremely difficult to obtain the best results from the huge expenditures of public money.

TABLE 71.—DEFICIT SPENDING AND THE INCREASE IN GOVERNMENT DEBTS, 1930-37

(Millions of Dollars)

	Dom- inion	Provinces and Municip- alities	Less Dupli- cations	Total
Capitalized Relief and Current Deficits.....	770	437	—	1,207
Capital Expenditures—not wholly self-supporting.....	147	477	5	619
Less—Municipal Contributions to Sinking Funds and Debt Retirement.....	—	199	—	199
Total Deficit.....	917	715	5	1,627
Increase in Cash and Liquid Assets.....	150	32	129	62
Total Increase in Outstanding Debt, 1930-37.....	1,078	747	134	1,659

Current Expenditures—rising debt charges, relief and other public welfare force contraction in other expenditures; important services in some provinces reduced below desirable standards

Relief and public welfare overshadowed all other government activities during the depression; aggregate expenditures of all Canadian governments on every other service, apart from net debt charges and defence, declined. If relief be

excluded the total per capita outlay of governments on current account was practically the same in 1937 as in 1930. However, this stability was entirely due to the decreasing expenditures of the municipalities. The senior governments assumed an increasing share of government costs; the Dominion-plus-provincial per capita outlay (excluding relief) rose slightly. While total government expenditures were not altered significantly they constituted a rising proportion of the national income, e.g., 20 per cent in 1930 and 26 per cent in 1937. Such increases of government expenditures as occurred were in connection with services (except defence) arising chiefly out of destitution caused by the depression. The per capita disbursements for public welfare (excluding relief) rose by nearly 60 per cent. As unemployment continued public health service had to be extended. The Old Age Pension scheme was adopted in four additional provinces and a rapidly increasing number of those over 70 were given assistance. After 1930 the Dominion increased its contribution from 50 per cent to 75 per cent of the cost of these pensions. During the eight-year period the outlay on old age pensions increased by \$27 million. The other significant rise in government costs, namely debt charges, was closely related to the capitalization of relief and other capitalized expenditures associated with the depression.

In 1930 relief and other public welfare absorbed 11 per cent of the current receipts; by 1937 the proportion had risen to 25 per cent. In the latter year these two items together with net debt charges took 53 per cent of the total revenues. The narrowing margin of the remaining income put a severe pressure on other government activity,

particularly that of the provinces and the municipalities. The per capita expenditures on education were reduced 16 per cent (in Saskatchewan there was a reduction of 41 per cent). The per capita outlay on the maintenance of roads and streets fell by 27 per cent on the average and by 41 per cent on the Prairie Provinces. In spite of the additional staffs required for expanding public welfare activities the cost of general administration was decreased, again the largest cuts being made by the Prairie governments. Thus the burden of relief which was left to the provinces and muni-

prices and luxury expenditures. About one-fifth of the total revenues (40 per cent for the Dominion) were obtained from customs duties on imports which fluctuated closely with the value of exports, capital movements and the volume of investment. Over 10 per cent of total government receipts was derived from imposts on cigarettes and liquor and was, therefore, sensitive to the wide swings which occur in the consumption of luxuries and semi-luxuries. Another 5 per cent came from amusement taxes, public domain, sales of commodities and services and from miscellaneous sources which were

TABLE 72.—GOVERNMENT EXPENDITURES ON CURRENT ACCOUNT, 1930 AND 1937—ALL GOVERNMENTS

(Thousands of Dollars)

	Municipal		Provincial		Dominion		Total ^(a)	
	1930	1937	1930	1937	1930	1937	1930	1937
Net Debt Charges.....	55,740	54,813	29,476	50,911	149,098	167,043	232,522	271,339
Defence.....	—	—	—	—	23,256	33,614	23,256	33,614
Pensions and Aftercare.....	—	—	—	—	55,341	54,437	55,341	54,437
Public Welfare.....	31,510	53,223	34,678	87,806	17,698	109,998	83,882	251,010
Education.....	84,705	76,606	33,775	32,121	702	272	119,191	108,899
Agriculture and Public Domain.....	—	—	21,241	20,636	23,298	17,909	44,484	38,545
Transportation.....	42,159	30,559	28,328	25,191	29,083	18,000	99,570	73,750
Subsidies to Provinces.....	—	—	—	—	19,036	21,210	—	—
General Expenditures— Justice, Legislation, General Government and Miscellaneous....	71,614	66,936	35,902	41,835	(b)70,332	55,685	(c)177,849	164,456
TOTAL.....	286,728	282,037	183,400	258,500	387,844	478,168	836,095	996,050

^(a) Includes Post Office Deficit—6,061.

^(b) Less duplications.

icipalities and the rising debt charges produced in many cases an undesirably large retrenchment in essential services. The upkeep of highways and buildings was skimped for the purpose of immediate savings which would later result in much greater expenditures. The outlay on public domain, particularly in British Columbia, was decreased to a point which hampered development and conservation of resources. Certain helpless groups such as the infirm were in some provinces inadequately cared for. The sums devoted to education in Western Canada were cut below those necessary for the maintenance of desirable standards.

Current Revenues—vulnerability of revenue structure, increases in revenue sought mainly by imposts on consumption and costs; inadequate use of progressive taxes on net incomes and inheritances

Canadian government finance entered the depression with a highly vulnerable revenue structure. A considerable proportion of the receipts were directly tied to the extreme variations of export

immediately affected by changes in economic conditions. Thus about 35 per cent of total government revenues were obtained from sources which fluctuated more widely than the national income. Between 1929 and 1933, this group of revenues fell by 53 per cent.

At the beginning of the slump, one-third of the public receipts consisted of municipal taxes on real estate which fell sharply in value as economic expansion ceased. Slightly over one-fourth came from corporation taxes, gasoline taxes, sales taxes, miscellaneous taxes and licences and fees. Less than 7 per cent was derived from progressive taxes on personal incomes and inheritances.

With the onslaught of the depression, governments were immediately harassed from two sides—rapidly falling receipts from vulnerable revenue sources and sharply rising costs due to relief, other public welfare and debt charges. The urgent problem of finding new revenues was greatly intensified by the wide differences in the decline of incomes in the various regions and areas and by the constitutional division of taxing powers. The

municipalities had virtually only one source of revenue—taxes on real estate. With this source nearly one-fifth of the relief and 14 per cent of the increase in other public welfare costs had to be financed. There were few places where savings could be made. Interest and sinking fund provisions respecting municipal debt constituted a large annual outlay that could not be reduced. These increases in cost and fixed charges made it impossible to avoid increases in levies and the maintenance of assessments. Due to the adoption of such increases receipts from real estate taxes declined only slightly in spite of rapidly falling earnings from real property. In the metropolitan area of Montreal levies on real estate were supplemented by a municipal sales tax. The sharp contraction of income from real estate after payment of taxes was an important deterrent to a revival of construction without which a substantial measure of recovery was not possible.

The provinces were restricted in their search for revenues both by the constitution and by practical circumstances. Indirect taxes were not within their powers. The income tax field was occupied by the Dominion. In any case, with the exception of Ontario, Quebec and British Columbia, the provinces could hope to get comparatively little from income taxes owing to the scarcity of large incomes and the prevalence of small-scale, individual enterprise in their economies. Although succession duties were imposed solely by provincial governments, revenues from this source could not be greatly expanded except in the Central Provinces because of the relative absence of large concentration of wealth in other provinces. Consequently increases were concentrated in the main on corporation taxes, gasoline taxes and motor licence fees. This group brought in over one-half of the \$70 million that was added to provincial revenues between 1930 and 1937. Income taxes were imposed by all the provinces except the Maritimes and Quebec, and the rates, along with those on inheritances were raised, but one-half of the \$25 million increase in receipts from these sources was collected in Ontario. The most hard-hit provinces ventured into new fields, Manitoba imposing a wage tax, and Saskatchewan and Alberta levying retail sales taxes.

The plight of some of the provinces was recognized by the Dominion by granting increases in unconditional subsidies. The special grants to Prince Edward Island, Nova Scotia and New Brunswick were increased by \$150,000, \$425,000 and

\$300,000 respectively in accordance with the report of the White Commission. During the same year British Columbia was given an additional \$750,000. In 1937, special temporary grants were made to Manitoba and Saskatchewan of \$750,000 and \$3,500,000 respectively to help finance essential government services which would otherwise have had to be continued at far below desirable standards. The total increase of \$7 million in the Dominion's unconditional subsidies, however, took care of only a small part of the increased provincial burdens. In 1937 large deficits on current account continued to exist in Saskatchewan and Alberta, and the other provinces were just barely in balance. However, few could long survive even a slight recession in economic activity without the reappearance of deficits.

The Dominion with its vulnerable customs and excise receipts was quickly confronted with the need to find new revenues. In 1931 the federal deficit rose to \$151 million (a figure almost equal to one-half of the total revenues for that year) and it never fell below \$74 million until 1937. In its efforts to raise additional income the Dominion resorted mainly to increases in consumption and corporation taxes. The progressive tax field was either left to the provinces, as in the case of the succession duties, or was not aggressively utilized. The sales tax was successively advanced from 1 per cent to 8 per cent. Corporation income taxes, excise duties on liquors and tobacco and revenue customs duties on a number of items of general consumption were sharply raised. Personal income tax rates were increased and exemptions lowered but not sufficiently to take care of more than a small part of the total requirements. Between 1930 and 1937 total Dominion revenues rose from \$314 million to \$464 million; almost three-fourths of this increase was produced by the sales tax.

The impact upon the constitutional framework of the exigencies of public finance during the depression added greatly to the confusion and inefficiency of the Canadian taxation system. The joint occupation by the Dominion and the provinces of the progressive tax field (except inheritance taxes) and the corporation tax field led in the one case to inadequate use and in the other to wasteful duplication. As a consequence far too great a proportion of the load of government expenditures was carried by regressive consumption taxes, by real estate taxes, and by economically harmful taxes on corporations and business.

TABLE 73.—GOVERNMENT REVENUES ON CURRENT ACCOUNT, 1930 AND 1937—ALL GOVERNMENTS
(Thousands of Dollars)

	Municipal		Provincial		Dominion		Total	
	1930	1937	1930	1937	1930	1937	1930	1937
Federal Subsidies.....	—	—	14,276	21,184	—	—	—	—
Taxes—								
Customs Import Duties.....	—	—	—	—	131,209	112,077	131,209	112,077
Excise Duties.....	—	—	—	—	57,747	52,037	57,747	52,037
Manufacturers' Taxes.....	—	—	—	—	10,474	17,185	10,474	17,185
Sales Taxes.....	—	4,412	—	1,893	20,147	138,055	20,147	144,360
Corporation Taxes.....	—	—	18,520	34,002	45,961	71,742	64,481	105,744
Succession Duties.....	—	—	20,780	35,757	—	—	20,780	35,757
Income Taxes on Persons.....	2,381	1,870	2,122	11,884	26,624	50,597	31,127	64,351
Gasoline Taxes.....	—	—	23,487	38,906	—	—	23,487	38,906
Real Property Taxes.....	257,118	244,936	6,708	5,875	—	—	263,826	250,811
Amusement Taxes.....	—	—	4,525	2,838	—	—	4,525	2,838
Other Taxes.....	23,275	20,337	1,534	3,005	4,531	7,391	29,340	30,733
Sub-Total—Taxes.....	282,774	271,555	77,676	134,160	296,693	449,084	657,143	854,799
Motor Vehicles, automobile licences, etc.....	^(a)	^(a)	19,907	25,937	—	—	19,907	25,937
All Other Licences, Permits and Fees, Fines and Penalties.....	11,294	10,454	10,024	8,905	3,703	2,539	25,021	21,898
Public Domain.....	—	—	17,037	21,135	2,297	2,484	19,334	23,619
Liquor Control.....	—	—	30,985	29,798	—	—	30,985	29,798
Sale of Commodities and Services.....	3,171	6,175	1,159	965	2,745	^(a) 6,269	7,075	^(a) 13,409
Other.....	19,916	20,881	2,759	2,390	8,608	3,948	29,457	25,733
TOTAL.....	317,155	309,065	173,823	244,474	314,043	464,324	788,922	995,213

^(a) Particulars not available; included with all Other Licences, Permits and Fees.

^(b) Includes Post Office Surplus—3,250.

CHAPTER VII
THE ECONOMY TODAY

1. CANADA'S PLACE IN THE WORLD ECONOMY

Canada holds a particularly important place in the world economy, or at least in that section of the world economy which has been, or remains, organized on a basis of interdependent trade and financial relations and which operates as a functional whole. Although containing less than one

¹In 1937 fourth in exports, eighth in imports, sixth in total trade.

per cent of the world's population, Canada ranks sixth among the leading world traders,¹ first among debtors,² fifth among creditors,³ third or fourth among security dealers,⁴ and first in tourist trade⁵—in fact she ranks high in all the major activities which make up the balance of payments.⁶ On a per capita basis the Canadian figures in all these transactions substantially exceed those of the leading world economic powers—United States, United

TABLE 74.—WORLD MERCHANDISE TRADE

Net Imports		Domestic Exports		Total Trade		
	\$ million		\$ million	\$ million	\$ per capita	
1. U.K.....	5,081	1. U.S.A.....	3,298	1. U.K.....	7,659	165.72
2. U.S.A.....	3,008	2. U.K.....	2,573	2. U.S.A.....	6,306	49.10
3. Germany.....	2,476	3. Germany.....	2,611	3. Germany.....	5,087	63.02
4. France.....	1,601	4. Canada.....	1,110	4. France.....	2,556	60.99
5. Japan.....	1,073			5. Japan.....	1,972	20.18
6. Belgium.....	923			6. Canada.....	1,919	174.01
7. Netherlands.....	853					
8. Canada.....	809					

¹Nominally, Canada is slightly exceeded by Germany.

²Approximately, based on the following estimates of foreign investments—

	\$billion
U.K.....	19
U.S.A.....	12
Netherlands.....	4
France.....	4
Canada.....	1½

Estimates for Belgium and Switzerland are not available.

³Complete statistics not available. The gross Canadian turnover is approximately \$1,000 million a year; this figure would be greatly exceeded by U.K. and U.S.A. transactions, and roughly equalled by Netherlands transactions.

⁴Foreign tourist expenditures in Canada were formerly less than in France, but in recent years Canada has apparently become much the largest tourist centre. It is interesting to note, however, that tourist expenditures in the State of California are double total expenditures in Canada.

TABLE 75.—CANADA'S BALANCE OF PAYMENTS

Current Account	1937		1938		1939	
	Credit	Debit	Credit	Debit	Credit	Debit
Merchandise.....	+1,009.7	-706.4	+847.1	-665.2	+933.6	-731.6
Gold.....	+ 145.1	- 0.1	+156.5	—	+184.4	—
Tourist Trade.....	+ 294.7	-124.4	+282.7	-121.0	+275.0	-110.0
Interest and Dividends.....	+ 78.8	-325.0	+ 66.0	-317.0	+ 53.2	-314.0
Freight.....	+ 111.7	-137.2	+ 79.6	-105.0	+ 86.0	-126.8
Miscellaneous Services.....	+ 25.2	- 63.9	+ 23.4	- 66.9	+ 29.1	- 69.9
Total Credits and Debits.....	+1,665.2	-1,447.0	+1,455.3	-1,275.1	+1,561.3	-1,352.3
Capital Account						
New issues and retirements of securities.....	+ 89.5	-177.9	+ 88.6	-150.5	+144.5	-234.7
Sales and Purchases of outstanding securities.....	+506.6	-511.4	+369.2	-340.3	+311.0	-238.9
Other capital movements.....	+ 24.0	-129.6	—	-129.0	—	-144.0
Net Outward Capital movements.....	+620.1	-818.9	+457.8	-592.8	+455.5	-617.6
Residual item.....	+ 19.4	—	+ 45.2	—	+ 46.9	—

Kingdom, Russia, Germany, France, Japan.⁷ The Canadian national income per capita was exceeded only by that of the United States in 1929, although in 1937, in part as a result of the drought, Canada was in sixth or seventh position.⁸ Industrially Canada is ranked eighth in the world (although only thirtieth in population); Canadian railways are the fourth largest in the world;⁹ and the volume of shipping from Canadian ports is about the fourth largest.¹⁰

These details are highly significant illustrations of the Canadian economy and of the role which Canada plays in international business. It is only by playing this role that Canada can maintain anything near her present standard of living and can support the great capital investment which has been made to equip her for this role. Because Canada is one of the least self-sufficient countries in the world her prosperity and her very existence depend on making the most of her own specialized resources, and on trading them as advantageously as possible for her other requirements. Her success will depend not only on her own skill and efforts, but also on the continuation of an interdependent and integrated international system of trade and finance. Everything which tends to restrict the operation of that system, such as barriers to the international movement of population, goods or capital, or the detachment and artificial isolation of large blocs from the world economy on a self-contained basis, reduces the scope for an advantageous international division of labour—the principle on which the existing Canadian economy and standards of living are built.

⁷But the per capita figures are higher in some smaller countries:

Per capita Gross Trade, in order of size of countries with larger per capita aggregate than Canada—1937

	\$
1. New Zealand	\$23-94
2. Belgium	214-93
3. Denmark	192-93
4. Norway	179-81
5. Netherlands	175-22
6. Switzerland	174-37
7. Canada	174-01

Source—Condensed Preliminary Report on Trade of Canada, 1938-39, pp. 46-48, and League of Nations Reports.

* NATIONAL INCOMES PER CAPITA, 1937

(In U.S. \$)

	At Present Exchange Rates	At 1929 Parities with U.S. \$
U.S.A.	536	536
U.K.	500	491
Australia	436	529
Germany	421	249
Sweden	380	398
New Zealand	412	503
Canada	377*	377

* Income Produced Method as estimated by the Bank of Nova Scotia as more comparable with incomes reported for other countries than Commission's calculations.

⁸Canada has the fourth longest railway mileage, ranking after U.S.A., Russia, and India, and the fourth largest ton mileage of traffic, ranking after U.S.A., Russia, and Germany.

¹⁰The registered tonnage of vessels clearing with cargo in 1938 (latest available year) was largest for the U.K., next for the U.S.A., next for France, and Canada was almost exactly the same as Germany, Spain, and Belgium.

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A very brief review of Canada's resources in relation to the international economy will make clear why Canada plays such a relatively large part in that system, and is so profoundly dependent on it. Canada can produce large surpluses of many agricultural products (cereals, potatoes, apples, cattle, pork, and dairy products), of many forest products (pine and fir lumber, spruce and poplar and balsam pulpwood), of many mineral products (gold, silver, copper, nickel, lead and zinc), and hydro-electric power more cheaply—i.e., with the application of relatively less capital and labour—than can be done in most other countries. On the other hand, either Canada cannot produce, or cannot produce as cheaply as some parts of the world, her own requirements of such essential industrial raw materials as iron, coal, oil, rubber, and tin; of tropical fruits, fibres, and other natural products; and of many iron and steel, chemical, and textile manufactures based on special local resources and techniques. Every country could display a list of surplus and deficit resources, but in few would both sides of the balance sheet contain such basically important products in such volume, and in few would the extremes be so great. Thus Canada is at once the world's largest exporter of wheat, newsprint and non-ferrous metals, and one of the world's largest importers of coal, oil and steel products. It is in this distribution and peculiar character of Canada's resources, and in her lack of resources, that we find the explanation for many of Canada's distinctive economic, and related public finance, problems.

Some of the salient characteristics of Canada's trade may be noted. Both the staple imports and exports are mainly bulky, relatively low-value articles, and the sources of supply are distant from the markets, and therefore cheap transportation is of vital importance. Of the chief staple exports, wheat required a very large capital investment in handling and shipping facilities and to-day requires an increasing capital investment in facilities for mechanized production. The forest and metal products, partly because of the technical character of Canadian resources, also required a very large capital investment in plant and in associated hydro-electric power developments. If these resources were to be developed at all, they had to be developed on the largest possible scale in order to secure the economies of mass production and to contribute to the support of the heavy initial overhead. But in order to achieve this end very large foreign markets were necessary; Canada produces five times her own consumption of wheat (excluding seed requirements

for export); ten times her own consumption of her chief forest product—newsprint; and twenty times her own consumption of her non-ferrous metal production. It is this surplus production which is necessary in order to bear the total overhead cost of developing these industries, and to keep unit prices down to competitive levels. As a result of this kind of development Canada now supplies about 40 per cent of the world export wheat market, two-thirds of the newsprint in the world export market, and 40 per cent of the non-ferrous metals in the world export market. Canadian production of these products is a very much smaller fraction of the total world production, and many countries, which are of some importance in the world market and consequently to Canada, are almost self-sufficient.

In other words, Canada, in spite of her comparative productive advantages, is pushed into the position of being a marginal source of supply for many of these commodities. If a country which is producing 90 per cent of its requirements and importing 10 per cent is forced, or deliberately chooses, to reduce consumption, the imported 10 per cent is likely to be the first sacrifice. Any substantial reduction in the proportion of the world market supplied by Canada is evidently bound to have profound effects on her ability to maintain competitive prices and support the huge investment made in expectation of large-volume production. In a period of world depression, of reduced purchasing power and of increasing trade restrictions, such as we have outlined in Chapter VI, the relative status of industries in this position suffers. There are weaknesses, not only because such a small proportion of their production is consumed domestically, but also because such a large proportion of the total international market is supplied by Canadian exports. Control of the marginal supply normally gives a bargaining advantage to the seller on a rising market, but reacts to his disadvantage on a falling market. The situation has been intensified by the continual narrowing of the international trading world in recent years, which has led to more abrupt and extreme price fluctuations than would occur in a broader market. When protected domestic industries develop in former markets, or when depression or war restrict demand for Canadian export staples, there will be excess productive capacity, and far more than the proportionate share of the excess capacity will inevitably appear in Canada.

The import staples, however, are in a somewhat different position. Large as are Canada's imports

of basic industrial raw materials (such as coal, oil and iron) in relation to Canadian consumption and even in relation to total world trade in these products, they are but a very small fraction of the total production, and of their consumption in the domestic markets of the chief producers. A fall in the Canadian demand is important, but is not likely to have the same shattering effects on prices as a fall in the foreign demand for the chief Canadian staples.

The great bulk of Canada's trade is with the United States and the United Kingdom. This is a natural corollary of the distribution of resources and organization of the economy in each of those countries and in Canada, and is intensified by the virtual withdrawal of most of the rest of the world from the former international trade system. Canada's geographical position and special relations with each of these countries are responsible for certain advantages and elements of strength, but there are also some liabilities. Canada's trade with both the United Kingdom and the United States is of vastly greater importance to Canada than their trade with Canada is to them; Canadian exports to the United Kingdom and the United States are between \$30 and \$40 per capita in each case, as compared with their exports to Canada of between \$2.50 and \$4 per capita. Canadian trade with the United Kingdom is 30 per cent of total Canadian trade, while United Kingdom trade with Canada is only 5 per cent of her total trade. Canadian trade with the United States is 50 per cent of Canada's total trade, while American trade with Canada is only 15 per cent of total American trade. This great degree of concentration of Canadian trade has elements of weakness and danger, and changes in the trading policies of either of the two large countries, or automatic changes in the terms of trade in response to differential price movements, inevitably affect Canada relatively far more than they affect the United Kingdom or the United States. Because of the greater vulnerability and lack of diversification, Canada's bargaining position is on occasion weakened and she is put at a disadvantage in opposing unfavourable policies or in negotiating for more favourable policies.

But quite apart from the danger of directly unfavourable policies, which may be due to factors quite unrelated to Canada but which may incidentally deal Canadian trade shattering blows, is the inevitable swing in the terms of trade. Canadian trade with both the United Kingdom and the United States is of a complementary nature, and is a classic example of the working of a basically sound international division of labour. While

Canadian cereals feed Britain, British textiles clothe Canadians; while Canadian products of the forest and mine, processed by hydro-electric power, feed the industries of the United States, the coal and iron products of the United States equip Canadian factories. But in any exchange of this nature there may be, and are likely to be, wide variations in the price trends of the various classes of products, and Canada may at any time find the prices of most of her exports declining more rapidly, or rising more slowly, than the prices of what she buys; or the reverse situation may result. Because her trade with the United Kingdom and the United States is relatively of much greater importance to Canada than Canadian trade is to those two countries, because of the much more specialized nature of Canadian exports, and because of the lack of diversified markets, variations in the terms of trade are much more important to Canada than to her two chief customers and suppliers. In times of depression both the United Kingdom and the United States can look to some important increases in the real value of their exports (and of their other income from abroad) to help temper the wind to the shorn economy, but Canada finds the impact of the depression intensified by the fall in the real purchasing power of the bulk of her exports. (In the last decade gold has been an important exception.)

In all other external transactions Canada is also vitally affected by the policy of the United Kingdom and, even more, by that of the United States. As we have noted, these transactions bulk extremely large in relation to total Canadian income. The large investments of British and American capital made to equip and exploit the economy; the contra investments of Canadian capital in foreign securities and enterprises; the integration of a large portion of Canadian manufacturing, finance, service and amusement industries with those of the United States; the huge seasonal tourist exchange, the periodic migrations of labour, farmers, and professional men and the continuous exchange of individuals; the existence of international labour, business and professional organizations; all these generate a continual ebb and flow of funds on a very large scale, and a continual process of adjustment of prices, costs, and profits. The transactions on account of the "invisible" items in the balance of payments on current and capital account with the United States are far larger than the total transactions on merchandise account, and in some ways may have an even more direct effect on comparative price levels, and thus

eventually on purchasing power parities. In some respects it is as difficult, and as artificial, to isolate the Canadian balance of payments as to isolate that of, say, the State of Pennsylvania, but in other respects there are Canadian policies in operation which do segregate the Canadian economy. These policies, however, cannot completely control the Canadian economy; they can only modify the impact of external influences on it. As has been indicated, these external influences are of great magnitude, and in experience Canada has followed virtually the full swing of violent fluctuations in the United States, modified only slightly by the greater stability of the United Kingdom. A vital difference in the impact of the notoriously abrupt and extremely fluctuating North American business cycle on Canada and on the United States is the substantially higher net income of the latter.¹² The relative fluctuations in business activity and in per capita income are approximately the same¹³ in the two countries, but the Canadian fluctuations occur around a much lower average income, and Canada lacks the impressive reserves of diversified climate and resources, and of a huge internal market which distinguish the United States. In short, Canada is compelled to accept the full measure of fluctuation which accompanies the highest standard of living in the world—without as high a standard of living to absorb it. There are certain physical and climatic disabilities and limitations which would appear to make higher costs and lower net incomes permanent conditions in Canada as compared with the United States.

Canada's balance-of-payment transactions, other than trade, tend to transmit the full extent of economic fluctuations in the United States to Canada, and there are also some special features arising from the nature of these transactions which intensify the pressure on the economy in times of depression. The most important item on the income side is that of tourist expenditures, which are luxury expenditures and likely to be drastically reduced in time of depression. On the payment side, the most important item is that of interest and dividend payments—a major portion of which is a fixed amount, and a large portion of which is due from Canadian governments. The dollar amount of this

¹² PER CAPITA INCOME
(Income Paid Out)

	Canada	U.S.
1929	\$470	\$679
1933	248	360
1937	345	536

¹³ 48 per cent decline in U.S. national income and 44 per cent decline in Canada's national income from 1929 to 1933.

payment can only be substantially reduced by widespread default, with all the long-run penalties which that entails, and in a period of falling prices the real burden increases. If in addition to falling prices there is also a fall in the exchange value of the Canadian dollar, the real burden of the large portion payable in foreign currencies increases even more. It is true that in the latter case there will tend to be a larger favourable balance on merchandise trade account, but the gains and losses will be unevenly distributed, and the increased burden of debt charges will put additional stresses and pressures on certain sections of the economy. In several years during the twenties Canada was on balance a capital exporter, and even in years when Canada was borrowing heavily abroad there was a cross current of Canadian investment abroad. But Canadian investments abroad went largely into equities, and often into merely margins of equities in the New York market, and into industries in Latin American countries which had economies every bit as vulnerable to world depression as that of Canada's. As a result Canada suffered heavy losses both on capital and income on her own foreign investments while she continued to meet the major portion of the debt payments due abroad. In the thirties favourable balances were used largely to retire Canadian debt rather than to make new investments abroad, and there has been an important reduction in the amount of outstanding debt payable in foreign currencies.

To summarize, Canada's position in both her trade and other financial relations with the outside world is largely that of her position in relation to the United States and the United Kingdom. This position is similar to that of a small man sitting in a big poker game. He must play for the full stakes, but with only a fraction of the capital resources of his two substantial opponents; if he wins, his profits in relation to his capital are very large, and if he loses, he may be cleaned out.

Canada's position in the world economy has both strengths and weaknesses. As long as it is correct to speak of a world economy, or even a partial world economy, in which any substantial measures of international division of labour and trade are permitted, Canada should enjoy a particularly high export income and national income, thanks to her possession of a few special resources. The provision of productive capacity to exploit these resources has involved heavy fixed charges; deficiencies in other resources and efforts to maintain past standards of living involve certain essential

imports on a large scale. We have thus a picture of a normally high income and of high fixed costs, but even under normal conditions the income is likely to fluctuate much more sharply than the costs. Because of the character of Canadian resources, and of the nature of Canadian trade and other financial relations with the United Kingdom and the United States, fluctuations in gross income, and consequently even more in net income, at either extreme of the business cycle reach relatively huge proportions.

It is scarcely necessary to add that if the international trading system in which the Canadian economy was designed and built as an integral part should be further restricted, a new appraisal (which would be distressing) must be made of Canadian resources and of the Canadian position. Our "boundless resources" are worth only what we can sell them for. If the system under which we exchange our surpluses for our requirements breaks up, our surplus and chief staple resources will cease to be resources; the whole structure of government and private investment based on them will collapse; and our conception of a "normal" or attainable Canadian standard of living will have to be drastically revised.

2. CANADA AS AN ECONOMIC UNIT

In spite of the fact that the major Canadian industries are a part of an international economy, certain national policies have been adopted and national responsibilities have been assumed which create a distinctively Canadian framework within which Canadian industries operate. The framework is not a simple structure, largely because national policies have been aimed at two major objectives—the expansion of export staple industries, and the development of a protected domestic economy—which, although they have sought to achieve a common national purpose, were directly opposed to each other economically. The compromises which had to be adopted to reconcile divergent interests frequently destroyed the logical symmetry of either policy. Nevertheless certain common conditions affect all Canadian industries and, in spite of basic divergencies in interest, there is sufficient homogeneity to consider the Canadian economy as a unit. It is the purpose of the present section to examine the framework of national policies and responsibilities, and the influence which they have had on the form of the economy.

In the preceding chapters we have described how and under what conditions that framework was

established. The events and circumstances which brought Confederation into being were not by themselves sufficient to ensure the maintenance of the union. In fact if the mutual interests and economic cohesion required for the growth of national unity, and the preservation of the political independence of the new transcontinental nation in North America were to be developed, the new Federal Government had the responsibility of devising and carrying out an appropriate economic program. It was necessary to link together the isolated regions with railways, to create a basis for internal trade, and to promote the development of the unsettled West as an integral part and a dynamic influence in the Canadian economy. It was for the accomplishment of these objects that the basic national economic policies of all-Canadian transportation, Western settlement and industrialization by protective tariffs were adopted during the first twenty years of the Dominion's history. These particular policies were not of course undertaken in response to any deliberate plan carefully thought out in advance to achieve the best possible results. They were rather the outcome of an evolution of political decisions which were strongly influenced by the requirements of politically workable compromises and by immediate circumstances. With a different course of events, perhaps a different set of policies would have been adopted to achieve the same general objectives. Perhaps a different set or a different emphasis would in any case have been desirable. That is not for us to say. We shall merely attempt to point out the significance of what was actually done (without going into all the day-to-day manoeuvres and detailed compromises which were necessarily involved) in relation to certain broad national aims, and the effect on the nature of the Canadian economy.

We have seen how the national economic policies were put into effect and ultimately achieved their purposes under the influence of the wheat boom and the demands of the Great War. Three transcontinental railways connecting the various regions across long and difficult stretches of unproductive territory were built at tremendous public cost in the form of direct assistance or guarantees. The West was filled with settlers whose products and purchases created a rising volume of traffic moving over the railways and waterways through Canadian channels. The protective tariff directed the demands of the great exporting industry on the Prairies to Canadian producers and promoted a rapid growth of manufacturing in Central Canada. Thus the hitherto isolated regions were drawn

together with an expanding flow of internal trade and economic integration. The transcontinental Canadian nation achieved a new level of prosperity, political security, and unity.

In the pursuit of these ends the three economic policies operated to effect a series of compromises which had a consistent objective; no one policy was complete in itself. Without the construction of all-Canadian transportation facilities and an appropriate structure of freight rates (and the huge public assistance which that entailed) each of the regions would have linked up with the railway systems of the United States. The connections between the various parts of the country would then have been made through the economically and politically aggressive neighbour to the south. This development would have been much less costly; it would have avoided the vast overhead of bridging great physical barriers; and it would have enabled the most intensive use of facilities already available. With the lower costs which this would have permitted, the export industries would have expanded further, the rise in the value of their natural resources would have been greater and the income obtained would have been larger. There would, however, have been no secure economic basis for a Canadian nation. Hence purely economic criteria were put aside for the creation and maintenance of a political entity. The same was true for the tariff, which in large part was complementary (although on purely economic grounds contradictory) to the settlement and transportation policies in the furtherance of this purpose. The railways and government assistance would have brought about the development of unsettled areas, but that by itself was not enough. Under free trade or with a much lower tariff the greater portion of the requirements of manufactured goods would have come from the United States. Each of the separate regions would have established its principal commercial relations with the external world rather than with the other regions. Traffic, excepting bulky exports for overseas, would have moved north and south. The tariff was designed to direct the demands into Canadian channels so as to provide east-west traffic to help support the vast overhead of the transcontinental railways and to furnish a stimulus to expansion in the older provinces who initially undertook the risks and heavy debts of the railway and developmental programs. Thus each of the three policies has exerted a consistent and an essential influence in the attainment of the national purposes. It is true that the tariff tended to

restrict the growth of exporting industries which the railway and developmental policies sought to promote. Some examples are worth noting of the ingenious compromises which have been developed in the tariff system in an effort to reconcile conflicting interests; a three-deck structure, and in some instances a four- or five-deck structure, has been developed to facilitate bargaining and negotiation with individual countries, and to aid the national transportation policies by directing traffic east and west through Canadian ports and over Canadian railways. Special exemptions are given for some of the machinery and supplies for the primary export industries (although not for construction machinery and other construction materials, and for some industries with differential advantages, such as hydro-electric power). The rates on manufactures are graduated according to the degree of processing and by giving greater protection on the final processing, assembling or finishing than the simple rate (which applies to the total value of the product) would indicate, attract and nourish branch plants from a great many American industries. Drawbacks provided for material used in manufacturing for export, coupled with individually designed provisions concerning the required manufacturing industries, give these industries an opportunity to compete in export markets (and reduce their overhead unit costs). Seasonal tariffs and artificial valuations for duty purposes are provided to protect domestic fruit and vegetable producers when their crops are ready to market. These and other special provisions vividly illustrate both the difficulties and compromises which were involved in applying a protectionist policy to the Canadian economy.

Without the higher costs imposed by the tariff the developmental policies would have been even more effective in stimulating the exploitation of Canada's resources for the sale of their products abroad, but that result, without the enhancement of internal trade, would by itself have weakened rather than strengthened the economic and political cohesion of the country. On the other hand, the tariff alone could have done little to create a basis for inter-regional trade without the markets provided by expanding export industries. Each of the national economic policies was by itself incomplete, and on purely economic considerations, contradictory to the others. Together, they have blended in a general policy which has built an economically integrated nation and they have on the whole sought to promote the realization of

consistent national objectives by which general prosperity and political unity could be achieved.

While the three national economic policies were in the main complementary, one or the other has at times been carried too far. The careful balance necessary for the attainment of optimum political and economic results from the major economic policies to which the country was committed has not always been maintained or appreciated. Mistaken optimism and regional pressures caused the over-extension of railways which has burdened the country with a needless overhead and encumbered the Dominion's finances with heavy fixed charges. The provision of essential all-Canadian transportation facilities would necessarily have involved large overheads and it was, therefore, all the more imperative that wastages should have been avoided.

For over forty years the Canadian tariff remained at a moderate level. During this period its provisions were gradually modified and adapted to the changing circumstances of the economy. The British preference was introduced, the rates on the implements of production of expanding export industries were reduced and special contrivances were adopted to enable the Canadian manufacturing industries to benefit from the technical and industrial progress of the United States. Thus on the whole no excessive restrictions were imposed on the growing export activities which constituted the basis of the economy, while at the same time a considerable manufacturing industry was built up. However, this careful balance and the cost price relationships which were established during four decades were suddenly broken by the sharp increase in protection during 1930-33. This unfavourable alteration in the circumstances of the export industries is particularly noteworthy since it occurred at a period when export prices were falling rapidly. The country was put into the position of carrying excessive debts incurred to promote the development of export production, while at the same time restraining the growth of such production by drastic tariff restrictions. Such extreme contradictions of policy were bound to reduce the real national income below what it would otherwise have been. Perhaps there may have been non-economic considerations which justified this high economic price. As debts pile up and the rate of expansion slows down the cost will become increasingly difficult to bear; it will place an increasing strain on public finance and consequently on Dominion-provincial relations.

While prices are rising and the national income is growing rapidly, overhead costs are easily borne and there is little conflict over the precise share of each region or industry in the total income. When prices are falling or the growth of the national income is halted, fixed charges and the weight of taxes arising out of extreme contradictions of policy may quickly become oppressive and there is likely to be increasing inter-regional friction with regard to those policies and the division of the total income.

During the first fifty years of Confederation the national economic policies operated as strongly cohesive influences in the Canadian economy. This success was mainly dependent upon the rapid growth of the wheat exporting industry of Western Canada. We have already recounted in Chapter V how during the twenties the unifying effects of these policies were weakened by the decline in the rate of expansion on the Prairies. With the onslaught of the depression this condition was greatly intensified. Drought and shrinking export markets for wheat brought almost a complete breakdown in the strongest dynamic factor making for east-west integration. Each area turned more than ever to the establishment of a more self-sufficient and independent regional economy. The possession of northern hinterlands with rich mineral deposits, the invention of new mining and metallurgical techniques, and water power have made possible the development of new northern frontiers for all but the Maritime Provinces. The separate regions established new contacts with external markets which rapidly decreased the relative importance of their economic relations with one another. In these circumstances the national economic policies were a limiting rather than an expansive influence. The railway policy no longer had any positive objectives. The new transport technique of the motor car has called for highway rather than railway expansion. Under these conditions leadership in the fields of transportation and development passed from the Dominion to the provinces. The Dominion was left to cope with the rising railway deficits.

The railway deficits were not the only consequences of the national economic policies with which the Dominion had to deal during the depression. When the industries which the national policies had helped to establish fell upon evil days, they naturally looked to the Dominion for assistance. The manufacturers called for higher protection against cheap imports. Western agriculture asked for relief and subsidized prices. The

Dominion could not completely avoid responsibility for alleviating distress of interests which it did so much to create. The implications of this are clear in the steeply rising expenditures of the Federal Government during the depression.

Thus during the twenties and thirties the national economic policies ceased to produce their former expansionary and cohesive effects and gave rise to a set of difficult national problems and responsibilities. Yet they could not be sharply reversed since the economic, and to a considerable extent, the political unity of the country was still basically dependent upon them. Furthermore, great vested interests have become established under their influences. The adaptation of these policies to the changing circumstances of the present and the future will require the highest qualities of statesmanship. Above all, the pursuit of objectives involving extreme and unnecessary economic contradictions must be avoided. Wastages must be minimized, particularly in the field of transportation where solutions to the problem of railway deficits and to the problem of highway and railway co-ordination have yet to be found. In the making of tariffs there must always be the clear realization that the economic welfare of the country is, and will continue to be, basically dependent upon the prosperity of the export industries. The problems of public finance and of Dominion-provincial relations in the future will be closely related to the extent to which these considerations prevail.

Monetary policy, in the broadest sense of the term, has only recently become a part of the framework of national economic policies which we are discussing. In the past, the policy of the gold standard had always been implied, and accepted unquestionably, as the only conceivable basis for development. This was virtually a required condition for a Canada which was part of an international gold-standard-and-trading economy, and it facilitated the rapid adjustment of prices and costs which was essential for a country in its position. The chief concern was the evolution of a banking system which would meet the very special and seasonal requirements of the Canadian economy within the framework of the gold standard. The highly centralized but elastic system of banks operating on a national scale which developed, was remarkably successful in this respect. It was only when the gold standard broke down and national currencies began to drift about in apparently aimless and alarming fashion that any question arose (and even then it arose some-

what belatedly) as to whether Canada needed a monetary policy of its own and adequate machinery to carry it out. The creation of a central bank provided the machinery, but conflict over the ultimate objectives of policy remained. The opposing forces were not, however, exactly the same as those engaged in the conflict over trade and tariff policies. Export industries generally stood to gain from a measure of exchange depreciation, while protected industries competing with imports were generally bound to do so. The lines of conflict were not clearly drawn on either a regional or an industrial basis; it was rather a struggle between owners on the one hand—owners of farm, mine, and forest resources, and of equities in industry, who depended on entrepreneurial net income—and recipients of relatively fixed incomes on the other hand—bond and mortgage holders and wage earners. Owners and debtors naturally favoured a higher price level; salary- and wage-earners and creditors, a lower price level. The very novelty of this division of interests, which cut across traditional class and regional groupings, delayed its recognition. Variations in individual circumstances also confused the actual issues at stake. We have noted how the wheat exporters, for example, in desperate straits in the thirties pressed for some measure of exchange depreciation although it was very doubtful whether under prevailing conditions it would have yielded any net advantage to them. Protected industries, on the other hand, which were much more likely to benefit were in general inclined to lean on the tried and proven method of increased tariffs (which was not available to the exporters) and, perhaps partly because of their close relations with large creditor interests, to view any experiments in inflation or exchange depreciation with suspicion and alarm.

But to-day much of the initial surprise and confusion has passed, and it is recognized that the purchasing power of the dollar not only can be deliberately altered but that it is at times expedient, and now considered almost respectable, to do so. But while the direct results of such action on individual interests are now more clearly understood, the effects on the economy as a whole, or sectors of it, remain largely matters of surmise. For one thing, these effects will depend on action (and reaction) in other countries; for another they will depend on the relative bargaining position at the time of the different interests affected, either favourably or unfavourably, and their ability to pass on the losses or retain the gains; and they will also depend on the nature of the other economic

polices adopted by the Government. But monetary policy has become one of the agencies by which the Dominion affects economic life and income in all parts of the country, and which makes Canada for certain purposes an economic unit.

Federal policies of taxation and expenditure form one of the most important groups of conditions which mould the development of the economy. These powers and functions have steadily grown in importance with the expansion in the scope of governmental activities, and it is important to note the manner and degree in which the public finance system in itself affects the economy and either stimulates or depresses the national income. The public finance system also provides a means of compensatory adjustments and transfers to counteract the adverse effects of other national policies. When, as a result of national policies undertaken in the general interest, one region or class or individual is fortuitously enriched and others impoverished, it would appear that there is some obligation, if not to redress the balance, at least to provide for the victim, and policies of taxation and public expenditure offer a convenient means. But as the field of public finance is shared by the Dominion with the provinces and their municipalities, the division of the field of taxation and the distribution of jurisdiction and hence of responsibility, have a major bearing on the equity and efficiency of the Dominion's public finance system, and of the public finance systems of all governments considered as a whole. For these reasons, and because of the basic importance of this particular subject to the Commission's inquiry, a separate chapter is devoted to a review of the present public finance system.

3. THE REGIONAL ECONOMIES

The international role of Canada and the national policies which have moulded the economy have been reviewed in the preceding sections and chapters. But as Canada is half a continent, she has very diverse regional characteristics and interests; and as a federation, she has different governmental systems for representing these interests and for carrying out regional policies of economic significance.

Economically Canada can be compared to a string of beads, and they are not all pearls. It is a long string in which the concentrations of productive resources are few and far apart. It has become traditional to speak of Canada in an economic sense as consisting of five regions,—the Maritimes, Quebec, Ontario, the Prairies, and

British Columbia, and in the main economic interests do tend to follow these regional lines. In many instances, of course, economic interests cut across regional boundaries—many sections of Quebec, for example, are more closely related economically to Saskatchewan than to neighbouring areas. Moreover, regional economies are constantly being modified,—Manitoba, for example, appears to be evolving toward the Ontario-type of economy, and away from the prairie-type. But each of the major regions has sufficiently distinctive characteristics to warrant separate discussion.

There is the more reason in view of the fact that the constitutional division of powers gives to the provinces important powers which may have a profound effect on the economy—control of the public domain, responsibility (implied if not express) for major social services and for local public works and highways, the power of direct taxation which has been broadly interpreted by the courts and which has been partly delegated to municipalities, and the power to borrow on the sole credit of the province. There is thus an important field in which each provincial government can influence its regional economy, and there are important functions in that economy which it must perform. The nature of the regional economy in each case is also of importance in determining the economic and public finance policies of a provincial government, and the degree of integration with, or conflict with, national policies that is likely to develop. It will be an advantage, therefore, to examine briefly the characteristics of the various regional economies and provincial economic policies.

The Maritimes

The Maritimes form the most mature, and the most chronically depressed, regional economy in Canada. Previous chapters have traced the long history of painful adjustment from the Golden Age, when wood and sail reigned supreme, to the present—a history in which the principal actors have been intangible but dynamic economic forces, playing on a stage set, and bounded, by national policies. Changing techniques and conditions of production, transportation and marketing affected the small but complex economy in diverse ways. A cross-sectional view today may indicate the factors which have determined the present economic position of the Maritimes, and suggest those which are likely to determine the future.

Perhaps the most significant feature, and one that has been an outstanding characteristic for a century,

is the delicate balance of the economy, resulting from the interdependence and complementary character of the chief industries. This interdependence arises from the nature of the Maritime resources and is such that no one major industry can suffer, as did the shipbuilding and carrying trade after the introduction of steam and steel, without profoundly affecting the whole structure. Cessation of one of the major Maritime industries has much the same effect as taking a wheel off a tricycle.

Agriculture in the Maritime Provinces is a mature industry, and the relatively small proportion of land suitable for cultivation has long been farmed.¹ In the proportion of arable to non-arable land Prince Edward Island is an exception but even here the average acreage in improved land per farm is less than in Ontario and Quebec. Owing to the topography of Nova Scotia and New Brunswick even in the best areas only small pockets or strips along river valleys are suitable for cultivation, and as a result cultivated areas are isolated from one another and farms are small² and often contain a considerable proportion of waste land. Thus, it is difficult in the general agricultural industry to secure the adoption of improved agricultural practices, the production of high quality products, the maintenance of uniform standards, or the provision of economical marketing arrangements—in short, to attain a high degree of efficiency in farm management. As a result of the small scale of operation and the economic disabilities this entails, the individual surplus available to the individual after subsistence is small. Notable exceptions to these generalizations are dairying and the production of certain specialty, export staples—apples, potatoes and fox pelts. These export staples are the chief cash products and are dependent on foreign markets, foreign tariffs, and foreign purchasing power. As a result the returns from these products fluctuate widely and on occasion disastrously. While total farm income, including income in kind, fell by half from 1928 to 1932, net cash income fell by four-fifths. Only the greater degree of self-sufficiency in agriculture, and the more numerous alternatives for employment—although at very low incomes—prevented duplication of the complete destitution of prairie agriculture.

¹ Of the total area, 36 per cent is in occupied farms, and 9 per cent in "improved land" (Census, 1931)—See Appendix—S. A. Saunders, *Economic History of the Maritimes*, pp. 56-60 (Miscographed).

² The average acreage of improved land per farm in the Maritimes (34 acres) is exactly half that per farm in Central Canada.

The primary industries most closely integrated with farming are forest industries and fishing, and these three F's form the basis for much of the processing and secondary manufacturing in the region. The farmer may work his wood-lot or, in areas where the pulp and paper industry or lumbering is of importance, work for the company on the annual cut during the winter months. Or he may combine farming and forest activities with fishing on his own account. In fact one-quarter of the farmers report their principal occupation as something other than farming (1931 Census) and one-sixth¹ of the gross agricultural income itself is derived from farm production of forest products.

In some respects forest industries and fishing fill the role of the frontier in the Maritime economy in times of depression. Individuals turn to these pursuits to augment or replace other income, since large portions of these industries are still organized on a basis of small, independent, and individual operation. In the fishing industry, for example, 10 per cent more were employed in 1933 than in 1929, and 20 per cent more in 1936, although total net income from the fisheries was two-thirds and one-third, respectively, less. The results of the interlocking relationship and great mobility of labour between the three key primary industries are, on the one hand, to communicate pressure on one industry very quickly to the others, but on the other hand to provide a degree of strength and insurance against complete destitution through the diversification and alternative employments provided.

The diversification is not as great as it might superficially appear, however, since farming, fishing and forestry have certain basic economic characteristics and disabilities in common and are all likely to be adversely affected by the same forces at the same time. The price structure and cash income of each industry is largely determined by uncontrollable developments in external markets and by foreign tariff and trade policies; the amount of assistance which can be given by national policies to the staple export industries when they are in distress has appeared in the past to be very limited; and the small scale and individualistic methods of operation has militated against securing the most economical and efficient methods of production and marketing and against the maintenance of high quality and uniform standards. With certain exceptions, such as the specialized apple, potato and fox industries where pre-eminent standards of quality have been developed, and the pulp and paper

industry where mass production methods can be applied, the Maritime economy in general labours under these disabilities, and they are reflected in a very low surplus income.¹

Manufacturing industries, which are based to a considerable extent on processing local raw materials, have suffered from the same disabilities, combined with pressure from the attraction of the larger markets of Central Canada for the newer industries, and from the depletion of some resources and from economic changes which have reduced the relative value of others. The relatively new pulp and paper industry is, however, a notable exception. National tariff policies have probably operated unfavourably in general, since Maritime manufacturing industries producing for home consumption have been exposed to the competition of the more advantageously located manufacturing industries of Central Canada; Maritime primary industries have been burdened with increased costs; and the great shipping, commercial, and financial service industries, which bulked so large at the time of Confederation, have either found it impossible to adapt themselves to changed techniques and the framework of national policies and survive, or have migrated to Central Canada. On the other hand, specific industries, of which coal mining and steel manufacturing are the outstanding examples, have benefited directly from national tariff policies and subventions for transportation, and special consideration in Dominion transportation and trade policies has been made for the benefit of the ports of Halifax and Saint John. Just where the balance lies cannot be precisely determined. To the extent to which the shift in manufacturing and service industries produced lower costs for Maritime consumers it was beneficial, but to the extent to which national policies made it impossible for the Maritimes to preserve and exploit whatever advantages they had, they were harmful. However, to a large extent the relative decrease in manufacturing in the Maritimes (from 13½ per cent of the gross Canadian production in 1870 to 4½ per cent in 1935) was simply a reflection of the passing of village-handicraft industry, and the concentration of industry in large-scale, highly mechanized units at the site most economical for production.

One important element of Maritime industry has received very large and important benefits from national policies—the closely related coal mining and steel manufacturing industries.² The Maritimes possess the only coal deposits on the North

¹ See Appendix 4—National Income.

² Seven per cent in Central Canada (1837) and negligible in the rest of Canada.

² One-fifth of the population of Nova Scotia is directly dependent upon its coal industries and subsidiaries.

Atlantic seaboard; of these the Nova Scotian fields are by far the most extensive and valuable. But their coal resources possess few other natural advantages. Because of the physical character of the deposits (half the tonnage is now raised from submarine mines, the seams are frequently faulted, and problems of raising, pumping, and ventilation are particularly important) operating costs are relatively high. In addition, the coal industry has had to face the same difficulties that have oppressed the industry the world over—the growth in alternative fuel and power sources (oil, natural gas, and hydro-electric power), and economies in the use of coal through improved processes and better equipment. The steel industry has also been adversely affected by the shift in demand from heavy railway steel to light consumers' goods, in which proximity to the market is a great advantage. The Dominion tariff on coal, the Dominion subsidies for coal used in gas and coking plants, the Dominion subventions for the transport of coal to Central Canada (which consumes nearly half the total Maritime output), the Dominion tariff on steel and special assistance to steel industries (which consume one-quarter of the Maritime coal) have alone made possible the maintenance of the industry on anything approaching the present scale. The transportation subventions and other direct forms of assistance of some \$2.3 million in 1937 were more than three times the amount of royalties and taxes collected by the provincial governments; the tariff of 75 cents per ton is approximately 20 per cent protection.

The alternative and diversified openings for employment and the small-scale individualistic character of business organization, which are so characteristic of the Maritime economy, have made mass unemployment and destitution less likely than in the more highly industrialized areas of Canada. Under the impact of unfavourable external factors whole industries may be reduced to very low levels, but still manage to provide a measure of subsistence. Certain specialized areas, such as the coal and steel district, are more vulnerable and their unemployed cannot readily find alternative employment at any level. But if unemployment has not emerged as a social problem on the same scale as in other parts of Canada, certain other social problems are more advanced. One is the greater proportion of elderly people who require assistance through old age pensions; another is the number of "special areas," such as the fishing villages, where chronic impoverishment resulting from years of continual economic pressure and difficulties in the industry is reflected

in inadequate education, public health, and other public welfare services; other problems are those of depleted and submarginal resources, and of inefficient methods of production and distribution, problems which call for research, economic planning and improved co-operative organization, whether through independent voluntary agencies or by governments.

Yet the very factors which create these wants reduce the taxable capacity of the area and make it difficult for governments to provide for them. Where such a large proportion of the income of the primary industries is income in kind, where the cash proportion fluctuates so sharply, and where there are no large urban, industrial, and financial concentrations of wealth and surplus income, the tax gatherer's problem is a difficult one. Too much of the Maritime industry is now in a marginal position to make an increase in taxation on consumption and costs desirable, and too few Maritime industries produce sufficient surplus earnings to make direct taxation on net profits and incomes remunerative.

Nevertheless, in recent years Maritime governments have undertaken a relatively huge and ambitious capital program designed to strengthen the economy and alleviate existing distress. In 1937 expenditures by provincial governments alone on capital public works equalled 7 per cent of the total "national" income in the Maritimes. These expenditures were financed by borrowing, largely from outside the Maritimes, and they have had profound effects on both the present position and future outlook of the Maritime economy and public finance system. The very large capital expenditures, chiefly on highways, have benefited the construction industry, and through it large sectors of the economy. Construction activities have absorbed virtually all unemployed employables in the area and have afforded part-time employment and cash income in some of the distressed agricultural areas. The provision of a modern highway system will also have important influences on the economy in the future. It is hoped that it will attract more tourist trade. It will certainly have an important impact on existing centres of distribution and on tributary supply and market areas. Whether it will produce a sufficient reduction in costs and sufficient increased income from new enterprises and extension of marginal activities to prove self-supporting in the long run is still impossible to say, but it is the most distinctive and important feature of the Maritime economy at the moment. Although a large number of industries and individuals and

the community as a whole have benefited from the program, and although aggregate figures of national income in the Maritimes have been prevented from falling proportionately as much as in other areas, it must not be overlooked that some groups and some areas, such as some fishing communities, have been reduced during depression years to distress scarcely exceeded in western drought areas.

To summarize, we find the Maritimes form a distinctive regional economy, with a large degree of self-subsistence and a very close and highly developed inter-relationship between the primary and many of the secondary industries, but largely dependent for cash income on a few specialized export staples which are extremely vulnerable to external conditions. The necessary small scale of operations in many industries, and the depletion of the best resources, are serious and continuing economic disabilities which are responsible for the low average income. The general effect of national policies has been to accelerate the natural shift of industry and finance, and of concentrations of wealth and income, to Central Canada, although specific industries (coal, steel, sugar, oil) have been bolstered up by tariff protection and other Dominion policies, and special assistance has been given the area by subsidizing railway freight movements and by subsidizing steamship lines, by diverting traffic to Maritime ports, and by extra subsidies to the provincial governments. At the moment the large capital programs of the Maritime governments themselves are the most important and stimulating governmental influences on the economy, but expenditures on the current scale cannot be continued indefinitely.

Quebec

Quebec contains such strikingly diverse regional economies that the area cannot be satisfactorily discussed in economic terms as a unit. Even provincial policies have had to adapt themselves to the differing regional circumstances, and consequently lack the simplicity and homogeneity found in some other provinces.

There are notably three distinct economies within the borders of Quebec. One is that which has grown around the Montreal metropolitan area, and which is one of the major integral parts of the transcontinental economy built by national policies. Montreal, it might be said, is the eastern bridgehead of the great east-west structure which connects the Prairies with the trade routes to the markets of the world. The major portion of Montreal's activities is based on handling and processing the staple exports (e.g., wheat to flour)

and the staple imports (e.g. raw cotton to textiles) of the country. Dependent on and tributary to these activities are many ancillary industries—the provision of land and sea transportation services and equipment, brokerage and banking services, local agricultural construction and supply industries, and amusement facilities. The Montreal metropolitan area, and the industrial towns and agricultural and resort areas immediately surrounding it, thus form an integral part of the international trading system by which Canada lives. The fortunes of the area are as closely dependent on the successful operation of that system as are those of southern Saskatchewan. The national policies of transportation and development were designed to bring direct advantages from the exploitation of western resources to this area, and, through the development of domestic markets, to bring further advantages to the manufacturing strategically located there and fostered by national tariff policies.

An economy of another type is that found in the vast area north of the St. Lawrence where a scattered number of huge, modern, highly-mechanized, pulp and paper and metallurgical plants process local resources with local hydro-electric power. These plants are almost entirely dependent on external markets, and on the maintenance of the existing international division of labour, but they do not form an integral part of the traditional national trading system and economy as does the Montreal area. Their connections with their markets are much more direct and simple, and although each unit has all the vulnerability of any highly specialized producer, they are not interlocked with and dependent on other factors in the national economy to the same degree. Perhaps their chief economic characteristic in common is their dependence on cheap hydro power, with consequent high capital but low operating costs.

The third type of economy characteristic of Quebec is the pioneer subsistence agricultural area. Some of the frontier agricultural areas (e.g., Abitibi, Lake St. John) are complementary and tributary to the neighbouring mass-production, export units of the mining and forest industries and should properly be considered as part of the highly specialized, electro-product economy previously noted. But there are many regions—the North Shore and the South Shore of the Lower St. Lawrence, Temiscouata and Matapedia, Gaspé and la Baie des Chaleurs, the Gatineau, Labelle, and Mattawinic, where mixed farming, usually combined with seasonal forestry or fishing operations,

yields a relatively low but self-sufficient livelihood. The cash income of these areas depends largely on the sale of a few staple products in either local urban or export markets, and on tourist trade, but the failure to develop, or impossibility of developing, any notable specialties restricts income in these areas in general to the yield of their rather limited and submarginal resources, which are worked on a small scale and often inefficiently.

The foregoing analysis cuts across the more conventional industrial classification, but may help to bring out the particularly complex problems of Quebec's diverse regional economies and their relations to the national economy and national policies. The problems of the agricultural industry in the St. Lawrence Valley, for example, are of quite different nature from those of agriculture in the Lake St. John area, or, from those in Gaspé, and provincial policies which might be appropriate and desirable in one case are not necessarily so in another.

The Montreal area,¹ with its dependence on the transcontinental economy built by national policies, enjoys a high degree of prosperity when the economy is functioning as it was designed to do, and it was the natural point to which the excess population of the subsistence agricultural areas gravitated. The continual increase in the urban proportion of the population, and the actual depopulation of some rural areas, caused concern in the twenties, but it was not until the depression of the thirties that the full consequences of this development became apparent. The depression in the export industries, which was rapidly communicated to the heavy capital goods and construction industries, to railway and shipping business, and to a lesser degree to consumers' goods industries, hit Montreal directly. The drastic tariff increases of 1930 helped to maintain employment in some of the secondary industries at the expense in the long run of the primary industries on which Montreal depended. But with the shutting off of emigration to the United States and the West, the pressure of the enforced rural exodus on Montreal was intensified, and a huge pool of unemployed, and largely unskilled, labour collected there. It

early became evident that unless progress along the traditional lines of Canadian expansion was rapidly resumed Montreal unemployment would become chronic and the hard core of the Canadian problem. When a measure of recovery in Canada did occur it came largely from expansion in new industries and frontiers which cut across the established national pattern and, although secondary Montreal industries benefited to some extent, the basic situation was scarcely alleviated. Unemployment in Montreal and the satellite industrial towns of the area became one of the outstanding economic and human problems of the time, and seriously threatened the solvency of local finances. Efforts to alleviate conditions by national policies were chiefly through tariff action, and efforts by provincial and local governments were through public works and back-to-the-land policies, but none of these proved effective on an important scale. Montreal steadily lost ground to the rival metropolitan centre of Toronto with its close relationship to the new and expanding industries. Since the Montreal area's great asset is its strategic position in a highly developed trading economy, and since its own local resources and commercial advantages in domestic markets are limited and inferior to those of some other centres, this decline in relative position, perpetuation of serious unemployment, depressed property values, and pressure on local services and finances would appear to be likely accompaniments of any general reorientation of policy from dependence on international trade to greater domestic self-sufficiency.

The mass-production, mechanized, export units of the Saguenay, St. Maurice, Gatineau, and Rouyn areas also have had their particular depression problems. In general volume of production was maintained, but whenever a large plant was closed down the whole structure of the local economy collapsed, local labour lost its only employment, local agricultural, retail, and service industries lost their market, the local government lost its financial basis. Even when operations were continued they were made possible by reducing prices to sacrifice levels at the expense of the wage-earners, the owners and creditors of the business, and the governments which depended on it for revenues, and in some cases important resources were depleted and sold at bare salvage prices. The natural advantages and technical efficiency of these large units were great, but their bargaining position in time of depression proved weak. Not only is the whole population of Quebec north of the St. Lawrence Valley (some 400,000) directly dependent

¹The Montreal area is used here to designate not only the Island of Montreal itself, which accounts for 60 per cent of Quebec's manufacturing, but also the industrialized area from Valleyfield to Lévis and Sherbrooke on the south shore of the St. Lawrence, which in general has much the same economic characteristics as Montreal industry, and produces some 17 per cent of Quebec's industrial output. Textile manufacturing is the chief industry, followed by the processing of food and metal products. There has been, in recent years, a notable decentralization and spreading of these industries throughout the whole southern section of the Province stimulated by lower labour taxation, and property costs in the smaller centres, and facilitated by the provision of electric power and highway networks.

on this highly specialized and vulnerable type of economy (which produces roughly one-quarter of Quebec's industrial output), but important groups of the supply, machinery, and construction industries, and of investors and financial institutions in Montreal and Ontario, are equally so. The process of applying mature techniques to Canadian virgin resources in this area requires a huge investment (i.e., huge in relation to the annual output) and in the short run, regardless of the efficiency of the techniques or the richness of the resources, the profitability of the investment depends on favourable conditions in uncontrollable external markets and on skilful marketing policies. When either of these conditions is absent it is not only the industry itself which suffers directly, but also the ancillary industries and dependent investments groups which make up an important fraction of the Canadian economy.

The third type of economy which we have noted is that of subsistence agriculture, chiefly on the frontier north of the St. Lawrence Valley and in the Lower St. Lawrence regions. The St. Lawrence Valley itself, which although only 5 per cent of the area of Quebec contains one-third of the occupied farm acreage and produces nearly one-half of the total agricultural production, is an integral part of the Montreal metropolitan economy. It is in this region that the most intensified and diversified agricultural output, the most progressive methods, the best markets, and the highest standards are found. The Abitibi and Lake St. John areas are largely complementary to the nearby mining, metallurgical, and pulp and paper export industries. The Eastern Townships are in a different category, and have declined as a general agricultural area under the pressure of competition from newer and richer regions, but have made efforts to adjust themselves to the production of some specialized products—live stock, dairy products, and maple products—in which they have some advantage or are at less disadvantage. The remaining agricultural areas are of the subsistence type, in which the production of hay, oats, potatoes and live stock for farm or local consumption is usually combined with wood-cutting or fishing to yield a small cash income. The limited and frequently inferior quality of the resources, and the production and marketing disabilities of small-scale and irregular operations result in very low income levels, and make it difficult for these areas to maintain their existing population, and much more so to absorb the natural increase when any alternative employment is accessible elsewhere.

Both because of the distress in these areas themselves and because of the pressure of emigration from them on the cities, much attention has recently been given their economic problems. The physical limitations of resources are admitted, but a more efficient integration of farming, forestry, fishing and certain rural handicraft industries might be worked out to advantage. By the extension of research and experimental work, field demonstration and education, provision in certain cases of improved credit and marketing facilities, and by assistance in improving and standardizing qualities of marketable products, some increase in the net income and standard of living in these areas should be possible. Improvement of conditions in the chief complementary industry would be particularly beneficial, for the greatest hope of any permanent progress lies in working out a satisfactory equilibrium between forestry and agricultural activities—"il faut chercher à marier l'économie forestière à l'économie rurale." But the results of very large and costly programs of colonization, rural resettlement and agricultural assistance in recent years would not suggest that this sector of the Quebec economy will ever attain a high level of prosperity or realize the hopes of those who look to it to replace the present dependence on nation-wide and international trade.

This observation is not intended as a criticism of the efforts which have been made to develop and assist agriculture since any alleviation of conditions in these subsistence areas resulting from improved methods and organization is of great benefit to the whole economy. It should also be recognized that there are other than strictly economic criteria. A self-sufficient rural economy may be preferred for various social reasons to a greater income-producing, more industrialized and urbanized economy integrated with the rest of the country and the world, and thus subject to external and uncontrollable blows and pressures. But from the economic point of view it is necessary to note the physical limitations to large-scale development of a self-sufficient rural economy which do in fact exist, and the impossibility, under any conceivable conditions, of its providing a satisfactory substitute for the nationally and internationally integrated economy which now supports four-fifths of the population.

Enough has been said to indicate the major disabilities and vulnerabilities of the Quebec economies, and the complex nature of the problem which governments must face in attempting to formulate economic and public finance policies. To a greater extent than in other provinces

economic criteria are on occasion subordinated to other social objectives, such as the maintenance of cultural values. As long as national policies worked to the advantage of the metropolitan area, as long as rapidly expanding markets were available for the new electro-product industries of the north, and as long as these two expanding sectors of the economy could help support the agricultural areas and absorb their excess population, there was a natural tendency for the provincial government to follow the let-well-enough-alone school of social and economic policies. Substantial portions of the cost of education and public welfare were left to the Church and the local authorities; the provincial government engaged in none of the public utility and other economic activities common in the other provinces; and a relatively larger share than in other provinces of the responsibility for highways was left to municipal governments. As one result provincial taxation, expenditure and debt were very much less (per capita, or in relation to provincial income) than in the other Canadian provinces although municipal and quasi-public institutional responsibilities were above the average. Another result was a tendency to ignore the potential social and economic problems which were an inevitable consequence of this type of development.

But when the combination of world depression and western drought of the thirties shattered the closely-integrated, national-trading structure, reduced markets and prices for electro-products, and undermined the elaborate financial structure of the economy north of the St. Lawrence, the Province was faced with a critical economic and social situation on all fronts. Governmental intervention on an unprecedented scale became imperative. In the metropolitan area it took the form of direct relief, public works projects, and assistance to back-to-the-land movements (in addition, of course, to the increased Dominion tariffs, which helped to maintain employment in some of the secondary industries). In the electro-product economy north of the St. Lawrence it included tentative efforts at enforcing cartel marketing organizations, exemption from certain public domain taxation, local highway and rural settlement programs, and direct relief. In the subsistence agricultural areas it consisted of increased research and technical instruction, cheap farm loans, increased premiums and bonuses to encourage improved production and marketing practices, and extensive direct assistance in the colonisation areas. The aggregate cost of these efforts proved staggering, yet they did little more

than tide the situation over, and made only a limited impression on the basic problems. Recovery in the United States and other external markets relieved the pressure on the export industries integrated with them, but the metropolitan area remained depressed. Unless the former trends of expansion of the transcontinental economy are resumed, or an internal stimulus comparable to the Northern Ontario gold mines is found, the most important sector of the Quebec economy will continue in the doldrums. This not only affects the other portions of the Quebec economy, but has far-reaching implications on the provincial public finance structure, on the responsibilities which the Province must be prepared to assume, and on the taxation system, which must support them.

Ontario

Ontario makes up such a large part of the whole Canadian economy that discussion of Ontario's salient economic characteristics frequently becomes a repetition of a description of the national economy. Ontario is not only the biggest but so outstandingly the wealthiest unit of the economy that its special advantages require some examination. Ontario has 33 per cent of the population of Canada, but (1937) 42 per cent of the national income, and from 45 to 60 per cent of the telephones, automobiles, residential electric power consumption, federal income tax payments, investment income received, government bonds purchased, and other evidences of higher than average surplus income and standards of living.

Ontario's advantages arise in part from her rich and diversified resources, in part from her strategic position in the national economy, and in part from her situation in relation to the industrial empire of the Great Lakes and Middle West to the south.

A lengthy catalogue could be compiled of Ontario's resources: the timber and pulpwood of the Ottawa Valley and Northern Ontario; the rich agricultural lands of Southern Ontario and the Ottawa Valley; the gold deposits of Kirkland Lake, Porcupine and northwestern Ontario and the nickel-copper deposits of the Sudbury area; the hydro power and the great avenues of transportation provided by her waterways; but note should also be taken of her lack of coal, iron, and oil. Within Ontario itself a very high degree of integration in the exploitation of her resources has been developed. The forestry, mining, and agricultural industries are all to some extent interdependent, and very closely related to the secondary manufacturing, service, and financial industries.

Although the latter industries depend on nationwide operations, the importance of their local market (and, in turn, their importance as markets to local agriculture) is great, and forms the basis of the greater development.

The character of the soil and the climate give Ontario agriculture the greatest diversification and the best balance in Canada. The ideal combination is possible of mixed farming which affords a basic subsistence and production of specialized staples for sale in either local urban or export markets to yield a cash income. The Ontario farmer has not, on the average, as high a cash income¹ as the Western farmer, but he has a very much greater degree of self-sufficiency, and his cash income is derived from a much more varied range of products—cattle and hogs, poultry and eggs, dairy products, tobacco, fruits and vegetables. On

TABLE 76.—INCOME PER FARM

	1928	1933	1937
PRINCE EDWARD ISLAND—			
Gross cash income.....	769	312	476
Net cash income.....	453	80	205
Income in kind—produce.....	264	141	186
NOVA SCOTIA—			
Gross cash income.....	419	328	433
Net cash income.....	141	128	193
Income in kind—produce.....	296	183	241
NEW BRUNSWICK—			
Gross cash income.....	411	220	350
Net cash income.....	132	20	108
Income in kind—produce.....	309	190	248
QUEBEC—			
Gross cash income.....	799	357	628
Net cash income.....	425	89	313
Income in kind—produce.....	379	219	293
ONTARIO—			
Gross cash income.....	1,400	673	1,115
Net cash income.....	838	255	643
Income in kind—produce.....	320	179	234
MANITOBA—			
Gross cash income.....	1,515	594	1,434
Net cash income.....	828	186	939
Income in kind—produce.....	225	133	185
SASKATCHEWAN—			
Gross cash income.....	2,341	538	627
Net cash income.....	1,614	66	141
Income in kind—produce.....	188	100	124
ALBERTA—			
Gross cash income.....	2,164	682	1,203
Net cash income.....	1,506	201	689
Income in kind—produce.....	178	109	164
BRITISH COLUMBIA—			
Gross cash income.....	1,093	614	905
Net cash income.....	460	184	353
Income in kind—produce.....	284	207	245

the other hand, his own subsistence production is more varied, and his cash income much higher than that of the average farmer in Quebec and the Maritimes. The primary agricultural industry thus contributes both an important stabilizing factor to the economy, and sufficient surplus production of marketable staples to serve as a basis for a profitable urban-rural exchange and division of labour.

Although these statements are generally true, it should not be overlooked that there are some agricultural areas, such as Huron and Bruce counties, which have been unable to meet Western competition in the production of their former staple or to find satisfactory alternatives. Some agricultural areas which depended on local mining markets or local lumbering activities as, for example, some in Eastern Ontario and the Ottawa Valley, or those about Cobalt and Gowganda, have been left stranded as the local resources were drained off. In other regions, such as the Rideau Lakes area, the Muskoka Lakes area, and the northern frontier, only small-scale, subsistence farming, combined with a little woodcutting, fishing and trapping, is possible, and in these, living standards are consequently very low and cash income, except where the tourist industry flourishes, virtually non-existent. On the other hand, in some areas such as the Niagara peninsula, specialization of production has been carried to a very high point, and in such cases fixed costs are high and net incomes consequently vulnerable and highly variable. But in spite of these exceptions Ontario agriculture as a whole, and particularly in the Western Ontario peninsula, is a well-rounded and basically stable industry which contributes importantly to the wealth of the Province and to maintaining Ontario in a leading position.

Ontario's lumbering industry was long the chief stimulus of the Ontario economy, and although the cream of the resources has been skimmed off and mining now takes precedence, pulp and paper production still plays an important role. Although the pulp and paper industry with efficient forest management and conservation methods could be a permanent and stable one, it still appears to be more profitable to the individual entrepreneur to gut the resources of one locality and move on. Whether this would be true if the industry were charged with the social costs of rehabilitating or salvaging the dependent labour and industries in the derelict areas, which are a necessary accompaniment of this practice, cannot be determined. But the development of conservation policies and

the achievement of greater stability within the industry would appear to be necessary if these resources are to be exploited to the best advantage and are to contribute to the support of the whole economy as they have in the past.

The last decade has seen a very large increase in Ontario metal production, due chiefly to the increase in the price of gold. Nickel and copper production have also expanded notably following the Frood discoveries in the late twenties, and as a result of improvement of processing techniques, increased production facilities, and the armament demand of recent years. But of outstanding importance has been the expansion of the gold-mining industry, both through extension of operations at the established camps of Porcupine and Kirkland Lake which still account for four-fifths of the total provincial output, and through the development of new producers in northwestern Ontario. The tripling in value of gold production during the decade affected not only the mining industry itself, the labour employed by it and the capital invested in it, but also a wide range of ancillary industries—transportation, power, lumber, machinery, chemicals and explosives, and the financial promotion and security-trading activities which have done so much to add colour and romance to Canadian mining development. Because this development occurred during a period of general depression it was of particular value and importance, and because it was closely integrated with Ontario industrial and financial centres and agricultural and forestry industries rather than with industries outside the Province, it cut across the traditional east-west lines of the economy and perhaps tended to weaken Ontario's interest in the economic welfare of the rest of the country.

So far we have only discussed those industries which make Ontario on the strength of its own resources a large and wealthy section of the economy. Provincial policies have played an important part in development, the most notable illustrations being the construction of the Temiskaming and Northern Ontario Railway which opened the mining areas; the Hydro-Electric Power Commission which furnished cheap power to industries, rural areas, and consumers in general; the Farm Loans Board which provided agriculture with relatively cheap credit; and the extensive network of modern highways which Ontario early provided and has maintained in good condition. These policies not only hastened and assisted the development of the Ontario economy, but also did much to shape the character of the development and to

integrate provincial industries and areas. The close relationship between frontier and metropolitan areas, and between primary industries and manufacturing and finance industries, creates a degree of interdependence which has its liabilities, but also makes for a diversified and well-balanced economy with inherent reserves.

But of at least equal importance with Ontario's natural resources are the strategic position Ontario occupies in the whole Canadian economy and the advantages which Ontario derives from national policies. Ontario's geographical position in relation to the rest of Canada, its resources, and its geographical position in relation to the coal and steel centres and the great industrial triangle of the central United States, made it the logical centre of Canadian manufacturing, and of the distributing, service, and finance industries which are dependent on industrial activity and urbanization. To the extent to which national policies stimulated this development, Ontario was the chief beneficiary. National policies stimulated the development in two major ways: aggressive policies of western development built up a market, and tariff policies directed the demands of this market to Ontario (and the Montreal area). Naturally the chief drive for this relatively advantageous combination of policies came from Ontario and Montreal. A special survey of 1,973 firms in 23 manufacturing industries in Ontario and Quebec, undertaken by the Dominion Bureau of Statistics for the Commission, revealed that between 25 and 30 per cent of their total domestic sales were made in the other provinces. Of course some of these sales would have been made without tariff protection, but on the other hand some of the sales in Ontario and Quebec would not have been made without tariff protection. Perhaps more direct evidence of the influence of the tariff in directing demand to domestic manufacturing industries (overwhelmingly concentrated in Ontario and the Montreal metropolitan area) is given by the 1930-32 tariff increases, which reduced the ratio of imports to the total value of production from 25 per cent in 1928 to 13 per cent in 1933.¹ This diversion of purchasing to the protected industries not only increases aggregate employment and income directly in the areas where they are located, but stimulates the development of satellite financial and service industries about industrial and metropolitan centres. A natural result of this concentration of industry and

¹ See Appendix 2—W. A. Mackintosh, *Economic Background of Dominion-Provincial Relations*, pp. 80-86 for details and for qualifications necessary in use of these ratios.

finance is a trend toward highly developed corporate, and frequently monopolistic, organization which in turn further stimulates the concentration of entrepreneurial and managerial incomes.

It has been noted that, in addition to the national policies which assisted in developing a market for manufactured goods in Western Canada and then directed the demands of that market to Canadian sources, proximity to the industrial heart of the United States has been an important Ontario asset. It has made available cheaply¹ the basic industrial raw materials of coal and iron in which Ontario is deficient; it has facilitated the introduction of new techniques and mass-production economies, and the rapid development of modern industries by making specially skilled labour and machinery readily available; it has encouraged the development of United States branch plants manufacturing for export to Empire or other countries where Canada may have preferential trading advantages; it provides an important tourist trade; it is on occasion an outlet for skilled and professional labour which cannot be absorbed in the Canadian market; and the industrial region south of the Border is an important source of capital for Canadian industries. In spite of tariff barriers there is some degree of integration and complementary specialization both in production and in the provision of public works between Ontario and the adjoining states which reduces overhead costs and increases net income.

One consequence of Ontario's dependence on the adjoining states for many of its industrial raw materials is that increased manufacturing activity in Ontario is bound to be reflected in increased imports, and tariff increases on finished goods tend to increase imports of industrial raw materials. In this process, of course, there is a diversion of purchasing from United Kingdom and United States manufacturers to United States industrial raw material producers, but Canadian exports are still necessary in order to provide the necessary exchange. The original dependence on Western wheat exports to provide this exchange has been diminished, as we have noted, by drought and adverse marketing factors in the wheat industry and by the rise of new export industries within Ontario. The importance of developments on the new northern frontier in power, pulp and paper, and gold is thus far greater than that of providing merely a new source of production, and a stimulus to Southern Ontario; it has become the basis for a

new pattern of economic organization cutting across the lines of the traditional transcontinental structure; it has tended to lessen the dependence of Ontario on the successful operation of the national system.

Nevertheless, there are weaknesses in the new structure which may have been concealed by its rapid expansion in a time of general depression. One is the exhaustive character of the gold-mining industry which is the mainspring of the whole development. Owing to the complex geology and structure of the chief deposits, estimates even approximately satisfactory of total ore reserves cannot be made as can be done, for example, in South Africa. There are, however, indications that both the Porcupine and Kirkland Lake camps have passed their zeniths. This is particularly important because, in spite of a 70 per cent increase in the gross selling price accompanied by some decrease in operating costs over a period of six years, no major new camp has been discovered. Some 80 per cent of the output still comes from Porcupine and Kirkland Lake, which have turned to the exploitation of former sub-marginal, low-grade ores to expand their production and prolong their lives. From the point of view both of owners and of society a large proportion of the returns from an industry of this nature should be treated as capital amortization, and the construction and capital equipment activities which it engenders must be recognized as non-recurring. Not only will the inevitable depletion of these resources reduce incomes directly and indirectly derived from them, but it will also create problems of social adjustment which will require extensive governmental intervention and assistance.

The wealth of the Ontario economy thus rests in part on a well-balanced and closely integrated development of its own natural resources, including its geographical position in relation to the rest of Canada and the United States. It has also depended in the past on the successful operation of the traditional national policies, which have combined with Ontario's natural advantages to divert a relatively large proportion of Canadian surplus incomes to advantageously located centres in Ontario. And in recent years it has been maintained by an intensive but ephemeral development of Ontario's own northern frontier. Whether or not it can be maintained in the future will obviously depend in part on the general prosperity of the Canadian economy, of which Ontario is such an important and integral part, and in part on Ontario's opportunities and ability to integrate herself with the Canadian economy in such a

¹In a prosperous year the states bordering on the Great Lakes produce 40 per cent of the world's steel.

fashion as to make the most of her natural advantages, and to protect herself against the potential disabilities inherent in her position.

The Prairies

The Prairie Provinces form the region most directly affected by major national policies. The major objectives of these policies in the past—to develop the virgin resources of the Prairies, and to provide for internal markets for other regions—were directly concerned with Western expansion, while they affected the rest of the country chiefly in accordance with the degree to which the other regions were integrated with and dependent on the Prairie development. We have also noted how other than purely economic motives determined national policies, and added to their cost—an addition which could be easily borne as long as the virgin soil of the Prairies and favourable world marketing conditions combined to produce an exceptionally high net income.

The rise of the wheat industry, on which the whole Western economy and an important part of the rest of Canada were dependent, was a classic example of the income and prosperity which an area with very limited resources could yield through international specialization of labour. Much of the population of Great Britain and the Continent could be better and more cheaply fed on Canadian wheat, and the population of Western Canada could be better and more cheaply clothed with European textiles than either region could provide from its own resources. But with the decline, and in some cases complete breakdown, of the international trading system which made such specialization possible, the Prairies threatened to become an equally classic example of an area doomed to chronic depression. The coincidence of widespread and recurring drought was the final blow, for it prevented resort to the traditional defence of the individual producer—expansion of production which, as long as actual operating costs were covered, would enable him even at very low price levels to spread overhead costs and compete aggressively in world markets. In addition the drought made necessary widespread subsistence relief for families and stock and provision of seed and other supplies which would normally have been locally produced. It has been attempted in other parts of this Report to give some description of the situation resulting from the combined effect of drought and the collapse of wheat prices. It is sufficient to note here that total income in the area fell almost by half, and income from agriculture by almost four-fifths, from the 1926-1929 average

to the 1930-37 average. These bare statistics, however, cannot convey the full measure of the Western débâcle with its shattering blows to living standards, to adequate nutrition, to health services, to educational standards, to community equipment such as highways, and to individual hopes and dreams and ambitions.

Although abnormal drought conditions are passing, the reduced world wheat market makes necessary a reappraisal of the whole Western situation and of the role of the West in the Canadian economy. The reduction in demand from Germany, Italy, and France alone, as a result of their policies of self-sufficiency, is roughly equal to the total surplus production of Saskatchewan; the effort to stimulate potato and root crop production in the United Kingdom, which is the one important remaining market, is directly aimed at reducing wheat imports; and the former dreams of expanding Oriental markets have been disturbed by the Japanese occupation of North China and its aftermath and by Canadian reluctance to accept Oriental goods in payment for exports.

In what is left of the international wheat market—say 500 million bushels a year as compared with the 750 million of the twenties—Canada's position is as strong as, or stronger than, it has ever been. Wheat producers in Australia, Argentina, and the United States have alternatives of production lacking in Canada, and Canadian producers have made notable advances in reducing their costs and improving their techniques. In the normal economic process Canada should gain a larger share of the reduced market. But this assumes a relatively lower level of wheat prices (excepting fluctuations due to crop variations) which will force marginal producers with alternative sources of employment out of wheat production. The implications of this for the Canadian West are that the better lands will produce a smaller net income than formerly, that much of the land occupied at present will prove submarginal, and that the possibilities of expansion are greatly reduced. In addition, we must take account of one of the factors which has been primarily responsible for reducing Canadian costs, and for enabling the West to compete with other wheat-producing areas—the mechanization of Canadian wheat farming, which greatly reduces the ratio of labour to acreage and production. But this development has left certain areas of the West with populations which, in relation to their resources, are excessive.

On the whole the wheat economy has reached maturity. It is a premature maturity owing to the general trend of international affairs, but from any

realistic point of view it must be recognized as a given condition for the present. The implications of this dénouement to the national economy are many. The overhead created on the assumption that the West would support a very large population, and the national policies which were based on the assumption that the West would provide a continually expanding market, are both threatened by the destruction of their original justification—the expectation of almost unlimited expansion of the world wheat market.

But the disabilities of the area must not be over-emphasized. Given a return of normal climatic conditions, the natural advantages of the industry are great, and there is some ground for hope that the United States will eventually provide a new and expanding market. But an economy accustomed to a rapid rate of expansion has suddenly to adjust itself to a long-term flattening out, or possibly even a measure of decline, in the basic trends.

Alternative outlets for employment and production are not hopeful.¹ Subsistence agriculture is possible in areas in northern Alberta and Saskatchewan, and eastern Manitoba, but the position of people dependent on subsistence agriculture in Western Canada is not encouraging. The volume and variety of local production in the West are limited by climatic and physical factors, and produce a relatively low standard of living. The lack of any marketable staple virtually eliminates cash income, and makes it impossible for these areas to secure any of the advantages of division of labour and specialization of production. From a social point of view they become rural slums, and centres of illiteracy and undesirable health conditions. From a public finance point of view they are potentially serious public liabilities in emergencies, and virtual ciphers at any time as contributors to public revenues. From the point of view of the economy as a whole, they contribute virtually nothing to the general overhead, while they exert a constant pressure on living standards in adjoining areas because of the enforced emigration of unskilled labour from them. So much has been said of the merits of self-subsistence agriculture and of developing a "peasant economy" on the northwestern frontier that it is necessary to refer to it. The most that can be said of it is that it can keep a certain number of people alive in deplorable living conditions. There are important exceptions to this sweeping generalization. Where there is opportunity for the development of some export staple,

such as hogs or alfalfa seed, which will produce some cash income, living standards may undoubtedly be improved and the community may make some contribution to the economic welfare of the region as a whole. But the possibilities of developing such specialties appear to be distinctly limited.

Mining development is also looked on as a possible alternative but it has so far been limited. It includes the exploitation of one large and a couple of minor complex base-metal ore-bodies in northern Manitoba, the development of the Turner Valley oil field, and the discovery of a few small pockets of precious metals in the Prairie sector of the Pre-Cambrian Shield. In addition persistent efforts have been made to develop the large but low-grade coal resources of southwestern Alberta and southeastern Saskatchewan, but the difficulty is the lack of a local market of any great importance. These developments should not be disparaged, and they have all contributed to maintenance of regional incomes and employment to an important extent during the depression, but it must be recognized that the greatest contribution of this type of activity is during the developmental stage, and that it offers no permanent solution for the economic difficulties of the Prairie region, as far as can be judged from our present knowledge of western and northwestern mineral resources.

Governmental expenditures are proportionately larger in an economy of the Prairie type than in a more self-sufficient one, but as cash incomes are also proportionately larger, governments with appropriately designed taxation systems have an opportunity to recoup. In time of depression governmental expenditures are larger because of the extensive need for aid when the staple export, and the primary source of income for the whole economy, collapses. In times of prosperity governmental expenditures are larger because of the economy and acceleration of development which result from financing public works and community equipment through governmental agencies. As a result Prairie governments have undertaken many economic activities—the provision of railways, electric power, telephones, farm loans, grain elevators, irrigation works—in addition to the normal provincial functions of roadbuilding and education. Even in these normal spheres governmental activity bulked larger than in the East. In a trading economy a highway and railway network is of first importance and, owing to the speed of Western settlement, transportation facilities had to be provided in a very short space of time. Educational costs have been increased by the similar need for

¹For extended discussion see Appendix by W. J. Waince, *Prairie Population Possibilities* (Mimeographed).

providing equipment speedily and the virtual absence of privately-endowed educational institutions.

It is obviously essential to all interests concerned to preserve the governmental structure and credit of Western Canada in view of the vital importance of community organization in such a vulnerable and specialized society. Whether the economic base of the governmental structure is wide and stable enough to finance the cyclical fluctuations of the chief industry of the region may be doubted in view of the extreme character of both the natural and commercial swings of fortune. In addition to the erratic course of regional income is another factor of great importance to Prairie public finance: the ability of the small, independently organized units of the individualistic, Prairie economy to bargain on equal terms with the monopolistic corporate organizations of Eastern Canada—to which the commercial relations of the area are largely restricted by national policies. The failure to secure advantageous terms of trade in the past has resulted in draining off the surplus income of the Prairies to the East and in efforts of the Prairie residents to use the economic powers of their provincial governments to redress the balance.

British Columbia

It is characteristic of the Canadian economy as a whole that rich concentrations of natural resources are separated by large barren areas, and in British Columbia this particular contrast is even more pronounced. Some of the mineral and forest resources are advantageously located on the coast, or in the relatively accessible Fraser River Valley, but many lie in the interior and can only be exploited after the provision of tremendously costly transportation facilities. Much of the Province is waste land, and even when some resources exist in pockets in these areas they are too distant or too difficult of access for profitable development. On the other hand, some of the Province's resources—the huge base-metal ore body of the Sullivan and many smaller deposits of gold, copper and coal, the stands of Douglas fir on the coast ranges, the rich agricultural lands of the Okanagan and lower Fraser Valley, the water powers of its rivers, the fine harbours of its coast, and the magnificent scenery of its mountains—are outstanding. The exploitation of these resources has on occasion yielded very large profits and has made possible the establishment of a high standard of living, including a high level of governmental services. But while the cost structure inherent in the geographical character of British Columbia

and the standards which have been adopted is high and rigid, the income to support it is extremely fluctuating. Added to the customary uncertainties and hazards of an economy partly dependent on mining, are the risks of dependence on foreign markets for a few primary staples which are subject to wide fluctuations in both demand and price, and access to which is dependent on favourable shipping rates.

External transportation is as vital to British Columbia as internal transportation. The opening of the Panama Canal and the chronic depression in shipping rates which followed the post-War boom brought British Columbia very much closer to the markets of the world. This not only produced higher net incomes for British Columbia producers, but greatly expanded the commercial possibilities of the resources of the Province, and extended the area which found it profitable to trade through Vancouver. For example, every cent reduction in ocean rates on wheat from Vancouver to Liverpool in comparison with the rate from Atlantic ports to Liverpool moved the border of Vancouver's tributary area further east, and finally all of Alberta and nearly half of Saskatchewan was captured. The movement of bulk exports from this area through the port, and even the return flow and distribution of import requirements, contribute relatively little to the economy once the flow is established, but the activity during any period of expansion is of great importance.

In the last two decades British Columbia has enjoyed a fortuitous coincidence of several factors of major importance. The great reduction in shipping costs which in particular stimulated the export of wheat by the Pacific and the development and export of lumber and later of newsprint, the improvement in electro-metallurgical technique which made possible the exploitation of the complex Sullivan ores on a huge and profitable scale, the expansion and rising demand in Prairie markets (until the drought) and particularly in the areas tributary to Vancouver, the rise of the tourist and resort trade, and the development of new Oriental outlets, each in turn engendered a huge capital program and all together stimulated an almost uniquely high rate of expansion which to some extent fed on itself. Vancouver rapidly emerged as an important metropolitan market, encouraging the development of secondary and service industries.

The depression revealed the vulnerability of the whole structure as United States lumber markets were closed, as base-metal demand and prices collapsed, and as new construction activity

dwindled. However, every primary exporting economy experienced much the same difficulties, and in the case of British Columbia there was some alleviation from the abnormally low ocean freight rates which improved its competitive marketing position and extended its tributary area, and from Imperial Preferential Agreements of 1932 and the Trade Agreement of 1935 with the United States. In addition, although the fixed costs of British Columbia industry were of necessity high, the operating costs of such important industries as base-metal mining, smelting and refining, and newsprint production, proved very low. As long as British Columbia enjoys below-cost ocean freight rates and retains important virgin resources to which the most modern and efficient techniques of production can be applied, it possesses a cushion in the most severe depression.

Nevertheless the acute depression of the thirties seriously threatened the financial solvency of the Government and, indeed, of the whole economy. It was a significant illustration of how precarious are an income and standard of living based on a few specialized resources and external markets, however profitable the combination may be in favourable periods. In addition, since some of British Columbia's most important resources are exhaustible and diminishing, since to some degree at least the high returns of the past have been achieved by treating capital depletion as current income, and since part of its expansion has been due to non-recurring capital development stimulated by the Panama Canal, it is evident that there are important problems and uncertainties in the future.

The special character of British Columbia's economy has influenced its public finances in many ways. The difficulties of transportation led the Government into the costly Pacific Great Eastern project which, if accrued interest due to the Province is included, accounts for half the present provincial debt. Geographical factors have also been responsible in part for the relatively small amount of municipally organized territory, and have probably inflated the cost of some governmental services. Even British Columbia's physical assets have their public finance implications; for example, the favourable climate attracts elderly retired people of means and thus augments the Province's succession duty revenues, but it also attracts unemployed transients and augments the Province's relief expenditures. Although the Government has incurred large developmental expenditures in order to make the Province's natural resources available, it has reaped a large

revenue from its public domain and corporate taxation. The resources are of a nature best exploited by corporations rather than individuals, and this has led to a concentration of taxable income and the adoption of appropriate taxation policies considerably and significantly different from those in other provinces. The high net incomes enjoyed during the skimming of the cream of the resources established high standards of living and services in general. In the depression there was approximately as great retrenchment as elsewhere in Canada, but this still left the majority of British Columbia services substantially above the rest of Canada in costs, and they could only be reduced to the Canadian average under the most extreme pressure. It is not suggested in any way that this would be desirable, but it is important to note it as one of the high, and in practice, uncontrollable costs of the economy. There are also other types of expenditure, of which the chief examples are conservation and research, which are temporarily avoidable and consequently usually suffer the major reduction in times of depression, but which are of basic importance to the future in an economy built to such a large degree on wasting assets.

4. CONCLUSION

We have noted some of the salient features of the Canadian economy and of the regional economies which have developed within the main structure. The Canadian economy is one which under any circumstances would have certain disabilities and weaknesses—the necessary dependence on a few specialized exports and the consequent vulnerability and sharp fluctuation in income, the large proportion of unproductive area and the seasonal handicaps which increase overhead costs, and the consequent rigidities of the cost structure as a whole. But in addition to those disabilities, which are inherent in the nature and distribution of Canadian resources, are the increased costs which have been incurred for political and national reasons and which further increase the rigidity and vulnerability of the economy.

From our survey of the economies of the various geographical regions it is also apparent that there are wide disparities in per capita regional incomes. This condition, as the historical survey in previous chapters indicates, has been more or less constant, but in times of depression it is likely to be greatly intensified at least as between certain regions. This condition raises grave problems of provincial and municipal finances; it militates against equality of

capacity as between provincial governments to withstand economic crises, and against equality of standards in provincial services, especially under the present division of revenues and responsibilities between the Federal and provincial governments. But the implications of this condition on public finance will be discussed at length in the following chapter.

There are clearly some elements making for national integration and interdependence, and some for division of interest and friction. With the passing of the period of expansion which was so greatly influenced by the traditional national policies, it may be necessary both for the preservation of national unity and the preservation of the national welfare that new policies should be inaugurated and developed to stimulate and give dynamic direction to new national expansion, although probably on very different lines and different frontiers. Several alternative policies are possible. In the vital field of external economic relations Canada might strive for closer integration with the United States, or with British countries, or for greater self-sufficiency. In internal management Canada might move toward a freer economy, with greater reliance on the unrestricted operation of the capitalist system and less responsibility for its casualties, or it might move toward a more controlled economy. A con-

trolled economy might increase or reduce the national income, depending on the wisdom of its policies and the skill with which they were carried out, and it might increase or decrease the existing unevenness in the distribution of the national income, depending on the prevailing philosophy as to the functions of government in this respect. The most appropriate policy at any time will depend on a variety of circumstances. One of the most important fields of national activity, and the one most immediately relevant to this Report, is that of public finance. It is impossible to forecast developments, but with the knowledge we now have of the vulnerability and weaknesses of the economy we know that our economic and fiscal policies must be adapted to meet current conditions and to prepare for possible emergencies. The Commission's task is not to say what policy should be followed, but, within the scope of its terms of reference, to recommend adjustments in the federal financial system which will make it possible to follow some policy. Canada's present and prospective economic condition makes it clear that we can neither continue to afford the friction and waste of conflicting policies, nor the greater loss due to paralysis of policy arising from a possibly obsolete division of governmental responsibilities and powers.

CHAPTER VIII
CANADIAN PUBLIC FINANCE TODAY

1. GOVERNMENT EXPENDITURES

Government expenditures in Canada have been equal to about 30 per cent of the national income in recent years. However, such a ratio is not valid as a measure of the "burden of taxation", or the "burden of government", for it may be highly misleading, particularly in comparison with that of other countries, and it must be qualified by analysis.

The various categories of government expenditure are of different significance: some expenditures are for the basic regulatory and protective functions of government; some are for collective services which the community believes it is advantageous to supply its citizens on a co-operative basis rather than to leave to private enterprise; and others are transfers from one group to another either on account of past obligations or to achieve some redistribution of the national income for social purposes. Any discussion of the relation of government expenditures to the national income must distinguish between these different categories. Expenditures on the first group of functions are necessary if the economic system, as we know it, is to operate at all. Expenditures on the second group purchase services which constitute part of the national income. Some of these services might have been purchased directly by the taxpayers had the Government not provided them. Or different services might have been purchased. It is not clear whether the intervention of government in these cases increases the national income, or decreases it, or merely changes its form. Expenditures in the third group are merely transfers which do not directly add anything to the income of the community as a whole, although they have long-run indirect effects which may be either stimulating or depressing.

Expenditures which may be considered as directly productive in relation to the national income include the cost of protection to persons and property, education, expenditures on development and transportation, and a portion of the costs of general administration and tax collection. These all represent the employment by government of labour, capital, and resources to supply services for the community. Expenditures of a transfer nature include direct relief, pensions, and other public welfare payments, and interest charges on non-

productive debt. Here no productive resources are employed and there is no direct contribution to the income of the country as a whole.

In 1937 out of a total government expenditure on current account of \$996 million, approximately \$406 million consisted of transfer disbursements. That is, between 10 per cent and 11 per cent of the national income was diverted into government channels and redistributed to the unemployed, war pensioners, old age pensioners, children, indigent sick, and on account of debt service on unproductive assets. (Of course, in a country of equal but more evenly distributed wealth, these transfer expenditures would be proportionately less needed.) The remainder of the government expenditures, \$590 million, are a measure of the value of the collective services provided the community by government and constituted about 15 per cent of the national income.

TABLE 77.—EXPENDITURES OF ALL GOVERNMENTS, 1937

<i>(Millions of Dollars)</i>	
<i>Collective Services:—</i>	
<i>(Including their share of debt charges.)</i>	
Primary functions of government (Administration, legislation, justice, and defence).....	213
Education	123
Development and Transportation.....	255
	590
<i>Transfers:—</i>	
Relief.....	127
War pensions.....	54
Other public welfare.....	125
Interest on unproductive debts.....	100
	406
	996
(The National Income, 1937.....)	3,829

The foregoing table merely indicates very briefly the relative order of magnitude of government expenditures in Canada. To review the chief characteristics of these expenditures a somewhat more detailed classification is necessary. It is first necessary to distribute the net interest payments (that is, the total amount of interest paid less interest received) of all governments according to the purposes for which the debts were contracted. The total outstanding debt (direct and guaranteed) of all Canadian governments was \$7,863 million at the end of 1937. Of this, \$1,413 million was represented by assets which were either liquid or self-supporting (or both). The purposes for which the remainder—\$6,450 million—was incurred are shown on the following table, classified according to the chief functions of government.

TABLE 78.—DEBTS OF ALL GOVERNMENTS WHICH WERE NOT DIRECTLY SELF-SUPPORTING^(a), 1937
(Millions of Dollars)

	Dominion	Provincial	Municipal	Total
<i>Outstanding Debt Incurred for—</i>				
1. Primary Functions of Government (Legislative, Administrative, and Judicial Buildings, and War Expenditures).....	1,818	80	x	x
Less cumulative current surplus before special charges.....	-1,233	—	x	x
NET TOTAL.....	585	80	225	890
2. Education.....	—	50	160	230
3. Development and Transportation (including Railways, Highways, Harbours and Canals, Power Commissions, Telephones, Agricultural Loans, etc.).....	3,250	975	275	4,600
4. Public Welfare (Relief, Public Health, etc.).....	420	235	175	830
GRAND TOTAL.....	4,255	1,340	855	6,450

^(a) These are the total debts, direct and guaranteed, of all Canadian governments less liquid assets (e.g., cash), investments which were completely self-supporting (i.e., which paid full contractual interest), and the capitalized value of interest earned by partially self-supporting assets.

The interest charges on this debt (ignoring for the moment any provision for amortization) were \$271 million, or about 27 per cent of all government expenditures. Approximately \$100 million of this interest bill was the cost of servicing unproductive debts, i.e., accumulated deficits, War expenditures, capitalized relief and capitalized

losses. The balance, \$171 million, was paid on debts incurred for public buildings, highways, railways, canals, and other developmental facilities which provide services for the community but which are not directly paid for by the individual users. In the following table of expenditures of all governments the net interest payments are distributed according to the chief functions.

TABLE 79.—EXPENDITURES OF ALL GOVERNMENTS, 1937

(On Current Account, before provision for debt retirement)

(Millions of Dollars)

	Dominion	Provincial	Municipal	Total
1. Primary Functions—				
Legislation, administration, and justice.....	52	33	x	x
National defence, military pensions and aftercare.....	88	—	x	x
Miscellaneous, less refunds and sale of miscellaneous services.....	—	9	x	x
Sub-total.....	140	42	65	247
Debt charges.....	23	3	14	40
Total.....	163	45	79	287
2. Education—				
Current Expenditures.....	—	32	77	109
Debt charges.....	—	2	12	14
Total.....	—	34	89	123
3. Development and Transportation—				
Agriculture and public domain.....	20	21	—	41
Transportation.....	20	25	31	76
Sub-total.....	40	46	31	117
Debt charges.....	128	37	18	183
Total.....	168	83	49	300
4. Public Welfare—				
Relief.....	66	43	18	127
Other Public Welfare.....	44	45	36	125
Sub-total.....	110	88	54	252
Debt charges.....	16	9	11	34 ^(a)
Total.....	126	97	65	288^(a)
5. Subsidies to provinces.....	21	—	—	—
GRAND TOTAL.....	478	259	282	996^(a)

^(a) After elimination of double counting.

Primary Functions

The expenditures labelled "Primary Functions" are the cost of the traditional forms of government activity, namely, protection to persons and property, national defence, and general administration. In the past these were virtually the only functions of government, but with the growing complexity of society, the increase in the scope for and the efficiency of collective effort, and the changed conception of the role of government in the amelioration of social distress, they have declined in relative importance. In 1937, including the heavy burden of the last War's expenditures (against which, for the purposes of this analysis, all current surpluses have been credited), they accounted for 28 per cent of total public expenditures in Canada.

The administration of justice, legislation and general government requires little comment. These functions may tend to cost somewhat more in a federal than in a unitary state, partly as a result of a certain amount of governmental overlapping and duplication, and partly as a result of the perpetuation of historical divisions and boundaries which have been made obsolete by the development of improved communications and transportation. It is easy to exaggerate the importance of these factors, however, and the detailed investigation made by the Commission of possible duplication of Dominion and provincial services,¹ and of possible economies from provincial union in the Maritimes and the Prairies,² revealed little avoidable expenditure.

¹ See Book II, Sec. C, Ch. II.² See Book II, Sec. C, Ch. I.

Defence.—The place and relative importance of national defence in public expenditures, on the other hand, depend on a variety of circumstances. In most European countries national defence has dominated public finance and has absorbed a major portion of governmental resources and efforts. Canada has enjoyed certain fortuitous geographic and political advantages which have profoundly influenced its national defence expenditures and, consequently, the balance available for other purposes. Before the Great War the cost of national defence was negligible, and it was this which permitted the extensive governmental aid to development and transportation which was such a striking and proportionately unique characteristic of Canadian public finance. Even after the War, including its legacy of debt charges and pensions, Canadian defence costs were still relatively low, although they had risen sufficiently to be a factor

in curbing the Dominion's developmental program. However, the quadrupling of current expenditures on national defence from 1935 to 1939 has altered the picture somewhat and has materially reduced the comparative advantage in this field which Canada formerly possessed, and on which many of her other public finance policies were based.³

Education.—Expenditures on education increased from before the War, indeed from the beginning of the century, in almost exactly the same ratio as all government expenditures until the early thirties. Education then bore the brunt of depression retrenchment and total budgets were cut by a sixth. There has been some expansion since 1936, but the total expenditure is still (1939 estimates) some \$10 million below the 1930 peak, and the ratio of education expenditures to all government expenditures has fallen from roughly

(*)TABLE 80.—CANADIAN DEFENCE EXPENDITURES COMPARED WITH THOSE OF OTHER COUNTRIES

For the fiscal years nearest to December 31, 1937

	United Kingdom ^(a)	U.S.A. ^(a)	France ^(a)	Australia	Argentina	Canada
Per capita defence expenditures (Canadian Dollars)....	27.26 ^(b)	7.89	8.43	3.46	4.52	2.98
Percentage of total government expenditures.....	26.1	13.4 ^(c)	18.4	7.0	14.6	5.8
Percentage of national income.....	5.4	1.4	4.1	0.8	^(d)	0.8

^(a) Only the published figures on defence expenditures were used in the calculations.

^(b) Includes expenditures authorized under Defence Loan Act, 1937.

^(c) Expenditures on Trust Account not included.

^(d) Argentine National Income not available.

15 per cent during the first thirty years of the century to 11 per cent in 1937, and somewhat less currently.⁴ It would not be realistic to assume

(4) TABLE 81.—PROVINCIAL AND MUNICIPAL EXPENDITURE

	1930	1933	1937
EDUCATION			
<i>Prince Edward Island—</i>			
Provincial and municipal expenditure on education (\$000).....	488	514	549
Per capita \$.....	5.55	5.78	5.90
Percentage of total provincial-municipal expenditure.....	32.7	31.8	27.7
Percentage of provincial income.....	2.1	3.8	3.1
<i>Nova Scotia—</i>			
Provincial and municipal expenditure on education (\$000).....	2,785	3,950	4,316
Per capita \$.....	7.37	7.57	7.78
Percentage of total provincial-municipal expenditure.....	26.0	22.7	23.0
Percentage of provincial income.....	2.3	3.7	2.7
<i>New Brunswick—</i>			
Provincial and municipal expenditure on education (\$000).....	2,823	2,619	2,675
Per capita \$.....	6.95	6.24	6.08
Percentage of total provincial-municipal expenditure.....	23.9	21.8	20.8
Percentage of provincial income.....	2.2	3.5	2.5
<i>Quebec—</i>			
<i>(Note discussion in the text of the contribution of the Church and of private fees in Quebec which makes direct comparisons with educational expenditures of other governments impossible.)</i>			
Provincial and municipal expenditure on education (\$000).....	20,201	22,566	22,701
Per capita \$.....	7.15	7.60	7.24
Percentage of total provincial-municipal expenditure.....	19.2	17.2	15.3
Percentage of provincial income.....	2.0	3.5	2.4
<i>Ontario—</i>			
Provincial and municipal expenditure on education (\$000).....	47,466	44,481	44,576
Per capita \$.....	14.03	13.48	12.01
Percentage of total provincial-municipal expenditure.....	27.2	22.2	23.2
Percentage of provincial income.....	3.8	4.0	2.8
<i>Manitoba—</i>			
Provincial and municipal expenditure on education (\$000).....	8,323	7,559	6,907
Per capita \$.....	12.31	10.06	9.63
Percentage of total provincial-municipal expenditure.....	26.1	19.4	19.8
Percentage of provincial income.....	3.3	4.4	3.7
<i>Saskatchewan—</i>			
Provincial and municipal expenditure on education (\$000).....	13,382	9,829	8,191
Per capita \$.....	14.80	10.55	8.72
Percentage of total provincial-municipal expenditure.....	20.8	21.8	17.6
Percentage of provincial income.....	6.8	7.8	4.2
<i>Alberta—</i>			
Provincial and municipal expenditure on education (\$000).....	11,715	10,069	9,447
Per capita \$.....	16.55	13.46	12.14
Percentage of total provincial-municipal expenditure.....	31.4	26.4	27.2
Percentage of provincial income.....	4.6	6.3	3.9
<i>British Columbia—</i>			
Provincial and municipal expenditure on education (\$000).....	9,788	8,257	9,365
Per capita \$.....	14.48	11.00	12.47
Percentage of total provincial-municipal expenditure.....	20.9	17.2	18.4
Percentage of provincial income.....	3.7	5.5	3.9

that this lower level will be maintained, nor from the evidence submitted to the Commission would it appear desirable. Since local governments bear more than three-quarters of the total cost of education, the most severe cuts in expenditure have occurred in the depressed areas. Yet it is in these areas that it is perhaps most necessary to maintain standards of education which will enable the younger generation to compete in all prospective fields of employment and which will thus assist desirable mobility of labour.

Transportation and Development.—The largest item in the expenditures of Canadian governments is that of transportation and development. Including current expenditures and net interest paid on debt incurred for these purposes, they account for nearly one-third of all government expenditures—a proportion that has scarcely varied since Confederation. The relative freedom from the burden of national defence, the geography of the country, and the extensive natural resources which could only be made available by the provision of extensive transportation facilities, have encouraged governmental promotion of economic expansion on a scale which is unique in capitalist countries. From the earliest days of responsible government the main objective of public policy has been the provision of transportation facilities and other public works which would stimulate the economic development of the country. The united Canadas strained their resources to construct canals and trunk railways in an effort to establish a commercial empire on the St. Lawrence. The Fathers of Confederation assigned to the new Federal Government the expensive task of uniting the colonies scattered across the northern half of the continent with railways, improved waterways and harbours. These projects were carried through at public expense or with public assistance to hasten the settlement of the empty spaces, to bring new resources into production, and to improve the inter-relationships between the various regions. More recently hundreds of millions have been spent on the construction of highways. In spite of the great economic expansion that has occurred it has not been possible, or at least it has not been deemed desirable, to charge the full cost of these facilities directly to users, and heavy burdens have been assumed by governments, mostly in the form of debt charges. Two-thirds of the total net debt charges are for interest on money borrowed for transportation and developmental purposes. While large expenditures have speeded up the economic growth and integration of the country, they have

also added to the difficulties of adjustment to fluctuations in so far as they have converted the relatively flexible costs of private industry into the more rigid costs of government indebtedness. In other words, the outlay on transportation and development constitute in large part overhead costs of the Canadian economy assumed by government—costs which would have been less rigid if they had been borne by private industry, in which case citizens would have sustained losses as investors instead of heavier taxes.

The major portion of these costs had to be met, in one form or another, if the Canadian economy was to be developed and a Canadian nation built; but the necessary burden has been increased to a substantial extent by misdirection of investment. In the past this took the form of unnecessary duplication of railway facilities; today it is being increased on an even larger scale in the form of duplication of, and lack of co-ordination between, all the modern agencies of transportation—railways, highways, waterways, and airways. The lack of co-ordination, even more than direct competition, is a cost and waste which Canada cannot afford today, and as discussed in Book II⁵ the problem is seriously aggravated by the existing division of jurisdiction and lack of unified financial responsibility. The rise of the automobile as an effective competitor in the most lucrative branches of short-haul revenue traffic has had far-reaching effects on the present position and outlook for railway finances (in which the Dominion Government is heavily involved); on the railway rate structure which evolved under very different operating and competitive conditions (and which subsidized the movement of low-grade, bulk freight at the expense of more valuable freight that is now being diverted to cheaper and more convenient channels); and on regional economies and vested interests of capital and labour which depend on the maintenance of existing transportation rates and differentials. In a country where cheap and efficient transportation is of such basic importance as in Canada, and where governments are already so very heavily involved,⁶ the rise of new agencies of transportation and major alterations in competitive conditions have profound effects on public finances. Although a great deal of study has been given in Canada to the railway problem and particularly to the relations between the two big

systems, relatively little attention has been given to the much broader problem of co-ordination of all agencies of transportation. The very fact that the existing division of jurisdiction makes it more difficult to deal effectively with the problem imposes greater responsibility on the governments concerned to attempt it.

Social Services.—Having noted the expenditures associated with the traditional functions of government, and the uniquely large Canadian expenditures on transportation and development, we come to the third major group of social service expenditures. These consist of expenditures for general public health, and, in larger and increasing amounts, for maintenance of individuals who cannot, either for physical or economic reasons, maintain themselves. The latter type of expenditure, and to some extent the former, are examples of the transfer type of expenditure which, in the same way as soldiers' pensions and interest on unproductive debt, redistribute the national income but do not directly increase or decrease it. Their rapid growth in recent years has effected a major change in the character of Canadian public finance, and has been responsible for the breakdown of the traditional division of financial responsibilities of the Canadian federal system.

The total expenditures of all governments on public welfare and relief (excluding soldiers' pensions) rose, but not notably more than all other expenditures (from 6 per cent of the total in 1913 to 8 per cent in 1929) until the depression, but then shot up to 25 per cent of the total in 1937. In dollars, expenditures quadrupled between 1929 and 1937.

It is not surprising that the huge increase in recent years has been generally looked on as an abnormal depression phenomenon, and that policies have been based on the wishful thinking that a return to prosperity would reduce the figures to pre-depression levels. As brought out in our previous chapters, however, fundamental changes were occurring and certain major forces operating which made very substantial increases in social service expenditures by governments inevitable even if a high level of general prosperity had been maintained. The increasing number of people in the older age groups (and the temporary, but at the time important, factor that some 60,000 of their potential supporters had been lost in the Great War); the increased specialization of the economy with its corollary of decreased local and family self-sufficiency; the growth of the cities and of the more vulnerable service and luxury trades;

⁵ See Book II, Sec. D, Ch. II.

⁶ See tables pp. 203 and 204. Outstanding debt of Canadian governments attributable to transportation and development \$4,500 million; current annual expenditures, including debt charges, \$350 million.

these were all normal features of a maturing economy. When, in addition to what we might call these normal economic changes which were operating to increase social service costs (although governments had not recognized them as normal and natural factors, and had not planned in any comprehensive way to make financial provision for them), Canada bore the full brunt of the world depression and of disastrous drought, government finances were particularly strained. The virtual inevitability, in any circumstances, of rapidly increasing welfare expenditures called for close examination of the governmental distribution of financial responsibility and of the appropriateness of the existing division of jurisdiction for administrative purposes, but when the depression expenditures were added to the already steeply mounting curve the need became urgent. It is important to distinguish between the increases in welfare expenditure which are directly due to the depression and those which would presumably have occurred in any case. The existing governmental framework and organization for public welfare purposes has proven woefully inadequate under depression conditions, but the present policy of meeting the situation by a series of *ad hoc* arrangements might conceivably be justified only if the new demands were of a temporary emergency character. If, on the other hand, the depression has simply intensified and brought to a head a situation which was developing in any case, and which the existing distribution of governmental powers and responsibilities had not been designed to meet, and has been proven incapable of meeting, a more comprehensive and constructive approach to the problem is necessary.

Public Welfare other than Relief.—Public welfare expenditures other than relief (including old age pensions, hospitals, asylums, public health and sanitation measures) rose from \$72 million to \$124 million between 1930 and 1937. To some extent, of course, this increase was due to the depression, but to some extent it was merely the continuation of a trend inevitably associated with the economic and social evolution of Canada. Old age pensions which were the largest item were introduced successively by all the provinces and it was discovered that there were both an increasing number of people over seventy, and an increasing proportion of those over seventy who were unable to support themselves (and whose relatives could

not, or would not support them).⁷ The provision of a minimum standard of subsistence and decency for the helpless and indigent aged is almost unanimously recognized as a proper and desirable function of government today, but it is a service which is open to serious abuses, and which may have far-reaching and quite unexpected results on the family and social structure. Certainly it was never contemplated, when the Act was introduced, that within twelve years half the population over seventy would be receiving its benefits. Whether the method which has developed of financing three-quarters of the total pensions by Dominion grants-in-aid has been conducive to the greatest possible measure of efficiency is discussed in the Commission's recommendations on the allocation of social service jurisdiction.⁸ The substantial transfer of the cost burden for this particular social service from municipalities to the Dominion government (relieving municipalities of the necessity of providing old people's homes and poor relief on the same scale as formerly) is only one, although the chief, example of a general trend of great significance. The distribution of public welfare (other than relief) expenditures between the three levels of government may be summarized as follows, and shows the greatly increased portion borne by the Dominion in recent years.

TABLE 82.—DIVISION OF PUBLIC WELFARE EXPENDITURES
(Other than Relief)

	1913	1930	1937
	%	%	%
Municipalities.....	53	40	29
Provinces.....	30	42	35
Dominion.....	17	18	35

In one of the Commission's research studies⁹ impressive statistics are presented of the economic loss to the country caused by ill health which is in many cases preventable. To the extent to which it is thought desirable, for both economic and

⁷Total Dominion, provincial, and municipal expenditures on Old Age Pensions. Estimated, on basis of continuation of same terms as at present, and of same proportion of population over 70 as used:

	(\$ million)	
	\$	\$
1927.....	0.3	1941..... 46.0
1929.....	8.5	1951..... 62.0
1932.....	17.0	1961..... 82.0
1937.....	29.0	1971..... 93.9

⁸ See Book II, p. 32.

⁹ See Appendix—A. E. Grauer, Public Health (Miscellaneous).

humanitarian reasons, to improve the health of the population there will be an increase in public health expenditures since the people who require attention are likely to be people who cannot afford it. In addition, it must be recognized that the public welfare expenditures, including both disease preventive services and institutions of several provinces are materially below the standards which are generally believed necessary and were formerly maintained. The general effects which an increase in expenditures of this nature are likely to have on the public finance situation are discussed in the following pages on relief. Certain increases in expenditure would appear likely simply because of the increased scientific knowledge we now possess, and the greater facilities in modern communities to provide for improved health services. Quite apart from humanitarian considerations, well directed expenditures on these services (and our knowledge and ability to direct these expenditures

are developing rapidly) should prove directly remunerative to the whole community.

Relief.—The various factors which have been responsible for the rise of the Canadian unemployment and relief problem have been developed at length in the previous chapters, and the present situation is discussed in the section dealing with the Commission's recommendations on the allocation of jurisdiction in social services. It is only necessary here to note the relation of these new expenditures to total government expenditures and their distribution.

From a negligible amount before 1930 (which is not shown separately in the Commission's summary of accounts since it was included with municipal poor relief under the classification of public welfare) relief expenditures (including relief works charged to capital account) rose to \$165 million in 1937. A brief summary of these is given below:—

TABLE 83.—TOTAL RELIEF EXPENDITURES (INCLUDING RELIEF WORKS CHARGED TO CAPITAL ACCOUNT)
(Millions of Dollars)

	1930	1931	1932	1933	1934	1935	1936	1937
A. Through provincial-municipal agencies—								
(1) Dominion share.....	3	34	34	28	43	41	52	55
(2) Provincial share.....	9	42	37	39	74	70	59	79
(3) Municipal share.....	5	16	21	23	23	24	28	18
Sub-total.....	17	92	92	90	141	134	134	152
B. Dominion expenditures through own agencies.....	1	5	3	8	17	39	26	13
GRAND TOTAL.....	18	97	95	98	158	173	160	165

The grand total expenditure on relief, on all counts, during the 1930 decade may be put at approximately \$1 billion.

Taking current account expenditures only, relief and other public welfare each accounted for one-eighth of the grand total of all Canadian government expenditures in 1937. These consequently provide transfer payments and a redistribution of income on a hitherto unprecedented scale in Canada. To an important extent the increased relief expenditures represent assumption by the state of responsibilities formerly borne by relatives—relatives who now cannot or, if given an alternative, will not bear them; to a minor extent they represent assumption by the state of responsibilities formerly borne by private charity; to some extent they are either an alternative or a supplement to very low paid labour, and in the latter case a form of subsidy to some employers. But in spite of individual abuses which have occurred, and the

unpredictable social and political effects of the major shift of responsibility for economic security from the individual and his family to the state which has occurred in the last decade, existing relief scales are rarely adequate to achieve their objective efficiently, i.e., to maintain the unemployed workers in a physically fit condition, and to ensure that their children are properly brought up. To some extent this is due to the lingering tradition that the individual should be responsible, in part at least, for his own welfare and that of his dependents; to some extent to the general practice of basing relief allowances on former poor relief standards, which were calculated with the object of maintaining non-workers alive, rather than of maintaining unemployed workers in good condition; to some extent to the fact that in the

early years of the depression many of the unemployed had certain reserves of their own—some savings, clothing and household goods, reasonably good health, etc.; and to some extent to the financial pressure on governments. Certain groups of the unemployed such as the transient and migratory labourers, and those who lived in areas where the local finances were in particularly bad condition, were worse off than the average, for no fault of their own, and suffered disproportionately and inequitably. Consequently, it is only realistic to assume that once the state accepts the responsibility of maintaining its unemployed under conditions which will keep them from becoming unemployable the cost will be higher than it has been in the past. (It must also be assumed that statutory minimum wages will be sufficiently above the relief scales to provide an incentive for work). On the other hand, it may be argued that the total cost in this case would be less than the present direct and indirect economic costs, to say nothing of the human values involved. Furthermore, organization of relief on a business-like basis would prevent many abuses and check many wastes which occur today.

The assumptions underlying this discussion are that unemployment, of some degree, is likely to be a permanent factor, and that the primary responsibility for maintaining the unemployed has become that of the state. Our economic analysis would suggest that the former assumption is now a probability, and, except under very unusual circumstances, a virtual certainty. The latter assumption, although representing a complete reversal of an earlier North American philosophy to which lip-service is still widely paid, has become, as a result of underlying economic changes, almost unconsciously but inevitably the ruling view. Given these premises the most important problem for the Commission is to determine how the responsibility can be most efficiently and equitably met. This problem will, however, be reserved for Book II.

The problem of large transfers of this nature, for which no immediate service is provided, is a new one in the Canadian public finance system, and because of the huge volume of the transfers (equal to total governmental expenditures in 1913) it is an extremely important one. Because of the breakdown of the accepted jurisdictional division of responsibility it has not been possible even to work out an efficient administrative technique to handle the problem. Even less has an approach been made to an understanding of the economic

factors involved, and to exploration of constructive policies and preventive measures, through co-ordination of relief policy with banking and exchange policies, public works, deficit financing and taxation policies, and commercial and industrial policies. Of particular importance for our immediate purpose, no thorough studies have been made of the effect of the great increases in transfer payments on the size and distribution of the national income and of the appropriate tax structure in relation to the new forms of expenditure which have been assumed. Nevertheless, there is an important relationship; it is clear, for example, that, once government has undertaken to provide a fixed minimum subsistence for a section of the population, there is substantial waste in imposing taxation—usually indirect taxation which requires the consumer to pay more than the government receives—on the same section of the population at the same time.

Social service transfer payments, and relief in particular, have been popularly singled out as the most significant public finance developments of the period. To critics of the philosophy underlying them they are a growing evil, to be tolerated in emergencies only in preference to the greater disaster of revolution; to supporters they are a means of achieving a new measure of economic security, greater justice, and greater happiness for the population as a whole; to governments they present new problems of fiscal as well as social policy, and a challenge that both the expenditures themselves and the accompanying taxation should be as efficiently and equitably organized as possible. Under the present division of jurisdiction and taxation powers in Canada, whose drafters could not, of course, foresee the development of this type of expenditure with all its corollaries, no effective approach by governments has been made to such a goal.

2. GOVERNMENT REVENUES

The revenues of Canadian governments are summarized for the approximate calendar year 1937 in the following table. It is extremely difficult to make a simple and realistic taxation classification. Neither the accounting division of itemized "tax" and "non-tax" revenues, nor the constitutional division of "direct" and "indirect" taxes has any particular significance or utility for economic description and analysis. Both these classifications have necessarily been developed, in great and precise detail, as useful tools for certain specific but limited purposes, and have, in their respective connections, acquired a pseudo-scientific weight.

TABLE 84.—REVENUES OF ALL GOVERNMENTS, 1937

(Millions of Dollars)

	Dominion	Provincial	Municipal	Total
GROUP I—				
Customs (ex. liquor).....	105	—	—	105
Excise (ex. liquor).....	32	—	—	32
Manufacturers Taxes.....	17	—	—	17
Sales Taxes.....	138	2	4	144
Gasoline Tax.....	—	39	—	39
Liquor Taxes and Profits.....	27	30	—	57
Automobile Licences.....	—	26	—	26
Amusement Taxes.....	—	3	—	3
Property Taxes on Improvements.....	—	3	112	115
Surplus Utility Earnings.....	7	1	6	14
Miscellaneous (Stamp Taxes, etc.).....	11	5	17	32 ^(a)
	337	109	138	584 ^(a)
GROUP II—				
Corporation Taxes.....	72	34	—	106
Company Fees.....	2	8	10	20
Public Domain.....	2	21	—	23
Business Property Taxes.....	—	—	14	14
Property Taxes on Real Estate.....	—	3	144	147
	76	66	168	310
GROUP III—				
Personal Income Taxes.....	51	12	2	65
Succession Duties.....	—	36	—	36
	51	48	2	101
Dominion Subsidies to provinces ^(b)	—	21	—	(a)
GRAND TOTAL.....	464	244	309	995^(a)

^(a) After elimination of double counting.^(b) Provincial subsidies to municipalities have been deducted from offsetting expenditures.

In Canada the distinction between "tax" and "non-tax" revenue is largely the reflection of the evolution of the technique of taxation which has been made necessary by the increasing complexity of the economy, constitutional difficulties, and the growing demands of government. When governments collected and spent a relatively small proportion of the national income, and when incomes were more evenly distributed, a revenue system of flat-rate licences, royalties, and taxation which approximated a per capita levy, was administratively the most simple; and it was adequate for its purposes without causing serious inequities or distress. But as more and more of the national income came to be collected and spent by governments such arbitrary methods of raising revenue became increasingly impracticable and inequitable. It became necessary to develop taxation systems which were more delicately adjusted to capacity to pay;—at first crude measurement of gross income was sufficient, but as government demands

increased in successive waves, refined measurement of net income became necessary. Whether the particular method employed was a graduated "licence" or a "tax" was simply an accident of historical nomenclature. Today a substratum of "non-tax" revenues, which are really specific taxes on selected objects, exists, but it has become an integral (although minor) part of the whole tax system. (Some "non-tax" revenues are in quite different categories. Fines, sales of services and commodities at cost, and interest earnings are not properly part of the public finance system at all, and should be netted against the corresponding expenditures. Trading profits, such as derived from provincial Liquor Commissions, are, however, highly developed forms of taxation from which the Government derives a combination in indeterminate proportions of a tax, based on capacity to pay and ease of collection, a fine based on the contemporary standard of moral values, and a business profit or loss based on the efficiency and judgment of the government enterprise.)

Originally, "direct" and "indirect" taxation were useful economic concepts. Incorporated in the British North America Act the terms became subject to interminable legal and political controversy. The courts were compelled to work out a definition which was broadly applicable in a formal way. In doing so they cited John Stuart Mill's definition as an authority, and developed it in meticulous detail. Today the "direct" and "indirect" taxation terms apply only to what the courts have held to be *intra vires* or *ultra vires* provincial jurisdiction.

In the foregoing table Canadian government revenues are listed in three groups. This listing is not a classification, for reasons which will be noted, but it may serve to bring out some of the distinctive features of the Canadian revenue system.

Group I consists of taxes on specific commodities paid, normally, by the consumers of these commodities. Group II consists of business and property taxes, which fall to some extent on ultimate consumers, to some extent on monopoly and scarcity-value rentals, to some extent on entrepreneurial net income, and in some instances on entrepreneurial capital.¹⁰ Group III contains the nominally "progressive" taxes—personal income taxes and succession duties.

Group I—Consumption Taxes.—Some of the limitations of this grouping should be noted. The first group which we may call consumption taxes, are in general regressive, yet individual consumption taxes may contain important elements of progressivity.¹¹ An obvious example of the latter case is the very high rate of taxation on certain selected luxuries, such as fine wines and liquors, which are presumably purchased chiefly by the wealthier classes. Even the general sales tax contains some element of progressivity as a result of the exemption of a number of necessities, although the exemptions are such that the incidence of the 8 per cent sales tax varies more between occupational groups—e.g., farmers and clerks—than between most income groups. Although there are modifications in the regressivity of consumption taxes made by special luxury

¹⁰ Property taxes (including interest on tax arrears) have been divided between Group I and Group II on the basis of the division of property assessments between land and buildings. The latter is estimated (complete figures are not available) as 44 per cent for buildings and 56 per cent for land. Taxes on buildings are treated for this purpose as consumption taxes; taxes on land as business taxes falling on monopoly and scarcity value rentals.

¹¹ A regressive tax is one which takes a larger percentage of a low income than of a high one; a progressive tax takes a larger percentage of a high income than of a low one; a proportionate tax takes the same percentage of all incomes.

taxation and the provision of exemptions on certain necessities, it must be remembered that these modifications apply only to expenditures on commodities. Expenditures on services and savings, which become increasingly important as income mounts, operate to reduce the proportion of consumption taxation to the total *incomes* of wealthier classes, although the proportion to certain categories of *expenditures* may increase.

In the lower income groups the 8 per cent sales tax may be estimated as taking from 3½ per cent to 5½ per cent of income, depending on the distribution of consumption. This is a very much higher proportion than taken by this particular form of taxation in other countries, but on the other hand, it is important and relevant to note that most other countries employ some form of payroll tax to finance at least part of their social service expenditures while Canada does not. It would not be strictly accurate to compare the sales tax with social service premiums and there is, of course, no relation whatever between the taxes paid and the benefits received by the individual. From the public finance point of view, however, it does extract about as much revenue from roughly the same class (in proportion to the taxpayers' incomes, and in proportion to social service expenditures) as social service premiums do in other countries—a fact which becomes of great importance when consideration is being given to the introduction of social insurance schemes. It would seem necessary to look on the sales tax at its present level as an alternative (and possibly an undesirable one) to social insurance premiums and not as a quite separate and independent revenue measure. It automatically provides for complete coverage (except in the cases of specified exemptions) and is relatively simple to collect, but has the serious flaw that consumers are required to pay more than the government receives, the difference representing the necessary mark-up in prices to provide for the higher overhead costs per unit on a smaller volume of business. It is impossible to segregate and earmark the amounts paid by low income groups.

It is not surprising that consumption habits will influence the amount of consumption taxation payable, but the extent of variation is notable. Individuals whose tastes run to beer, cigarettes, and movies (or to champagne, cigars, imported tweeds and super-charged cars), will pay proportionately several times as much in consumption taxation as abstemious citizens. Such comparisons illustrate the inevitable use of the powerful instrument of taxation for economic, social, and even

moral, as well as fiscal, objectives. Certain contradictions and clashes which arise in this process are important from the fiscal point of view. To the extent to which taxation is successfully used, for alleged moral or economic reasons (e.g., as a punitive deterrent to drinking whiskey, importing foreign goods, going to horse races, or accumulating large fortunes) it fails to raise revenue. When non-fiscal criteria become of dominant importance in shaping taxation policy, not only are new complexities and inequities introduced, but unexpected strains are thrown on other parts of the system. The outstanding example, of course, is the customs tariff which, to the extent it becomes protective, ceases to be revenue producing. Similarly, tobacco and liquor taxes (which in Canada yield considerably more than all personal income taxes) are frequently footfalls of conflicting policies. Of less clear but possibly greater economic importance may be the effect of very steeply graduated income and succession duty rates, which have been established at penalty rates on very high incomes and large inheritances for other than purely fiscal reasons.

Group II—Business Taxes.—The business and property taxes listed in Group II not only possess highly diverse characteristics at any one time, but frequently alter in kind at different stages of the business cycle. Normally, a substantial portion of these taxes—say property taxes, public domain revenues, and perhaps one-third of corporation taxes—may be considered a levy on the rental values arising from scarcity of land and other resources. As long as business conditions are such as to justify the existing capitalization of these resources such taxes are not burdens on costs, but simply the transfer to society of the increase in incomes which has been created in large part by the development and expenditures of organized society. But if the earning power, and therefore the rental value, of these resources decline without a corresponding fall in taxation these taxes become a capital levy. Some of the business taxes (i.e., the fixed taxes on corporations) are normally consumption taxes, but, as in the case of other consumption taxes, under some conditions and for relatively short periods of time they may be absorbed by the producer. The remaining portion of corporation taxes are flat-rate levies on corporation net income. As this income belongs to the shareholders, such a tax (which is not permitted as a deduction from the income tax of the individual shareholder) is both discriminatory between different classes of assets (e.g., as between bonds and stocks) and, according to the principles of

progressive income tax rates adopted in personal income taxation schedules, inequitable as between different income levels. On the other hand, it may be argued that this special levy is discounted in the market price of corporate securities, and that people who have purchased corporation securities under the existing tax rates suffer no relative disability. The special taxation on corporate profits may, however, have a significant effect on investment, and from the point of view of the individual investor may be sufficient to tilt the balance in favour of hoarding or bond investment as compared with investment in equities, or to influence a company promoter to bond his company to the limit rather than to finance by common stock.

It is unfortunate that the taxes in this group cannot be more precisely classified. Virtually their only common characteristic is that they are levies imposed at some intermediate point in the production-consumption cycle and are peculiarly subject to shifts in incidence as general business conditions change. Some of these shifts are on occasion highly inequitable and have disastrous economic effects (e.g., the shift in property taxation during a period of falling land values from a levy on socially created surpluses to one on capital). It is perhaps this group which should be particularly subject to constant review in framing the most desirable tax policy, and in which indiscriminate increases during periods of depression are likely to have the most harmful general effects. We have noted, however, that the existing constitutional straitjacket has virtually forced provincial governments into arbitrary increases of substantial amount in this form of taxation in recent years.

Group III—Progressive Taxes.—Personal income taxes and succession duties in Group III are (with the exception of straight proportional levies such as the special Income Tax in Manitoba), progressive taxes falling on surpluses (i.e., income in excess of that necessary for subsistence), and cannot, with very few exceptions, be shifted. It is only in this group that the final incidence of taxation can be exactly determined and delicately adjusted (presumably a *sine qua non* of equitable and efficient taxation), but it must be noted that the exemptions provided and the rate of progression are frequently determined by non-fiscal and non-economic influences and political pressures. Too little is known at present of the ultimate economic effects of different rate-curves and changes in these taxes to set up any objective economic criteria, and the need for planned

research as a guide to Treasury policy is evident. The tremendous importance of these forms of taxation as instruments of social as well as fiscal policy makes it impossible to eliminate what may frequently be conflicting influences, but much would be gained by distinguishing and setting out the various factors as clearly as possible.

Characteristics of the Canadian Tax System.—The fact that more than half the total governmental revenues and expenditures are local and provincial makes it difficult and somewhat unrealistic to discuss as a whole, as if Canada were a unit, the incidence of the Canadian taxation system, the services provided by government, and the resulting transfers of income. However, complex and occasionally confused and conflicting as the Canadian tax structure is, there are some outstanding characteristics.

The system as a whole, as compared with that in other countries, is highly regressive, with the qualification that it is very steeply progressive in the higher income groups. As consumption taxes make up nearly 60 per cent of total government revenues (which in turn, it will be remembered, equal some 30 per cent of the national income), and as various forms of business taxes make up another 30 per cent, only 10 per cent of total government revenues are in forms to which any scientific principles of progressivity can be applied in order to redress the regressivity inherent in the heavy Canadian consumption taxes. Further, three-quarters of this 10 per cent comes from personal incomes of more than \$10,000 and proportionately large estates and 35 per cent from the \$50,000 a year group and over; the Dominion income tax on very large incomes is one of the highest in the world, and the combined Dominion-provincial tax in the four Western Provinces is perhaps the highest. When the combined Dominion-provincial income tax reaches such figures as 105 per cent of the total income (as in Alberta, for example, on an income of \$1 million), the principle of progressivity has been carried to a fantastic extreme. Between the very wealthy man who is carrying one of the heaviest income tax loads in the world, and the very poor man who is carrying one of the heaviest consumption tax loads in the world is the large middle income group which escapes relatively lightly. It is primarily by adjustment of the income tax curve of progressivity that this trough in the curve of progressivity in the tax system as a whole can be removed, and the extreme impositions at each end of the curve modified. The present situation

appears inequitable, although it must be admitted that it is impossible to define "equity" in this instance in absolute terms. Equity as between income classes is basically a matter of social philosophy, and it must be left to the political crystallization of the prevalent philosophy to determine, for example, whether taxation should be progressive, and if so, at what rate.¹²

But in this connection it is important to note the obstacles to the use of the income tax as an instrument of either social philosophy or efficient fiscal practice which are presented by the existing division of tax powers and the joint occupation of the field by the Dominion, provincial, and even municipal governments. In Book II¹³ a table is given showing the amount of income tax payable by residents of each province on incomes of \$3,000, \$10,000, and \$100,000. On the last income¹⁴ the tax payable to Dominion and provincial (or municipal) governments varies from 33 per cent of the total income in Nova Scotia (Halifax) and Quebec (Quebec City) to 58 per cent in Saskatchewan (Regina). In addition to such substantial differences between the amount payable, there are major differences in exemptions and in determination of taxable income in different jurisdictions.¹⁵ Quite apart from considerations of the apparent inequity of these variations is the fact that the joint occupation of the field makes it mechanically impossible to develop an income tax which will, in itself, apply to different income groups in what is currently considered an equitable manner, and which can be adjusted to the desired degree of progressivity of the tax system as a whole.

Another outstanding characteristic of the Canadian tax structure is the high proportion of taxation on costs, as contrasted with the low proportion of taxation on surpluses and net incomes, and the amount of taxation of a character which is likely to be shifted from surpluses to capital or costs in times of depression. Taxation which falls directly on business enterprises, as such; taxation which is based on an arbitrary capitalization of income which does not, in fact, materialize; taxation which increases the costs of living at a subsistence level, and which consequently either increases wage costs and the costs of operation of farmers and other individual entrepreneurs in the

¹² See Book II, Sec. B., Chap. VIII, for a discussion of equity and efficiency in taxation.

¹³ Section B, Chap. III, p. 111.

¹⁴ Prior to the September 1939 increase of 20 per cent in Dominion rates.

¹⁵ See Book II, p. 158, for illustration of effect of double taxation of income in Western Provinces as compared with Ontario practice which exempts Dominion tax paid from the provincial definition of taxable income.

long run, or forces living standards of large portions of the population below the minimum desirable level;—all these are taxes on costs. The alternative is taxation designed to fall on the income of individuals which is in excess of that necessary for subsistence. This brings up the whole problem of the "efficiency" of the present tax system. "Efficiency" in its most narrow sense might be interpreted as economy in collecting the existing taxes. In a broader, and far more important, sense it is skill in collecting a given amount of revenue with the least possible burden on the national income. In both senses the Canadian taxation system fails. Duplicate taxation machinery, inadequate and divided jurisdiction (involving cumbersome and expensive devices to do indirectly what the constitution prevents from being done directly), and lack of uniformity, all contribute to unnecessary expense and reduced returns. Of immensely greater concern, the lack of co-ordination in tax policies, and the almost uniquely high proportion of the Canadian taxation burden on costs rather than on profits, reduce the Canadian national income seriously. The national income is depressed in both a positive way, through restriction of marginal investment, production, and employment, and in a negative way through obstruction of the use of fiscal policy as a stimulant. These are criticisms partly of general

taxation policy, and partly of the current working division of taxation powers between the different levels of government. To what extent the latter is significant will be examined in more detail.

3. FEDERAL DIVISION OF REVENUES AND EXPENDITURES

It seems generally accepted that it was the intention of the Fathers of Confederation, and indeed the only basis on which the Dominion could be built, that the central government should possess the revenues and carry the expenditures which were national in scope, while to the provinces and municipalities should fall the revenues and expenditures of provincial or local nature. The difficulties lie in translating at any given time these general principles into terms of specific taxes and responsibilities, and, when the appropriate revenues and expenditures fail to balance, in providing for adjustments, without infringing on the autonomy of each government in its proper sphere. As our historical review has developed, an additional difficulty has been the changes in the character of many governmental responsibilities and revenues as the economy evolved, and as governmental activity and the public finance system expanded.

TABLE 85.—DIVISION OF GOVERNMENT EXPENDITURES BETWEEN THE DOMINION, PROVINCES AND MUNICIPALITIES, 1937

	Share of each Government in Total Expenditures				Percentage Distribution of each Government's Expenditures			
	Dom.	Prov.	Mun.	Total	Dom.	Prov.	Mun.	Total
1. Primary Functions^(a)—								
National defence, military pensions and aftercare.....	100	—	—	100	23	—	—	11
Legislation, administration justice and miscellaneous.....	31	25	44	100	12	18	28	18
Sub-Total.....	57	16	27	100	35	18	28	29
2. Education^(a).....	—	28	72	100	—	13	32	12
3. Development and Transportation^(a).....	56	28	16	100	35	32	17	30
4. Public Welfare^(a)—								
Relief.....	54	33	13	100	17	19	7	15
Other.....	28 ^(b)	37	35	100	9	18	16	14
5. Subsidies to Provinces.....	—	—	—	—	4	—	—	—
Total Debt Charges^(c).....	(52)	(19)	(20)	(100)	(35)	(20)	(20)	(27)
Total.....	48^(d)	26	28	100	100	100	100	100

^(a)Including debt charges.

^(b)Excluding \$8.9 million to maintain annuities reserve.

^(c)Already included in previous items.

^(d)Including subsidies to provinces.

In 1937 nearly one-half of all public expenditures was made by the Dominion Government. Almost 60 per cent of the total federal outlay is in connection with national defence, the provision and maintenance of railway and waterway facilities, and development, all of which are essential national functions for which the Dominion was established. Another 12 per cent of Dominion expenditures is devoted to legislation, justice, and general administration, 4 per cent goes to unconditional provincial subsidies; and the remainder, 26 per cent covers relief and other public welfare. With the exception of the latter there are no noteworthy departures from the original conception of the purposes of the Dominion. Public welfare has been generally regarded as the primary responsibility of the provinces and municipalities. In the preceding chapters we have described how, under the pressure of circumstances, the Dominion was obliged to take over an increasing share of public welfare and relief costs. The manner in which the Dominion has assumed some of the financial obligations for these services, however, constitutes one of the weakest features of the Canadian public finance system. Although the Dominion pays for 44 per cent of all public welfare costs (75 per cent

of old age pensions and 54 per cent of relief) it has very little control over the outlay of its funds or over general policy since the expenditure of the money and administration remain with the provinces and the municipalities.

The provinces and municipalities each take care of slightly more than one-fourth of the total costs of government. They provide nearly 70 per cent of the total outlay on the primary legislative, regulative, protective and administrative functions. Almost three-fourths of the total cost of education is dependent upon the highly decentralized revenue sources of the municipalities; the remaining 28 per cent is obtained from the somewhat broader sources of the provinces. Prior to 1914 by far the greater part of the burden of transportation and development was carried by the Dominion. With the coming of the motor car and the decline in the rate of national expansion, a rapidly growing portion of these responsibilities fell upon the provinces. At the present time highways, streets, outlays borne by the provinces and municipalities to support local industries and to encourage the exploitation of provincial resources, constitute 44 per cent of the total government expenditures on transportation and development. However, the

TABLE 86.—DIVISION OF GOVERNMENT REVENUES BETWEEN THE DOMINION, PROVINCES AND MUNICIPALITIES, 1937

	Share of each Government in Total Revenues				Percentage Distribution of each Government's Revenues			
	Dom.	Prov.	Mun.	Total	Dom.	Prov.	Mun.	Total
GROUP I (Chiefly Consumption Taxes)—								
Customs (ex-liquor).....	100	—	—	100	23	—	—	11
Excise (ex-liquor).....	100	—	—	100	7	—	—	3
Manufacturers' Taxes.....	100	—	—	100	4	—	—	2
Sales Taxes.....	96	1	3	100	30	1	1	14
Liquor Taxes and Profits.....	47	53	—	100	6	12	—	6
Gasoline Taxes.....	—	100	—	100	—	16	—	4
Automobile Licences.....	—	100	—	100	—	11	—	3
Property Taxes on Improvements.....	—	3	97	100	—	1	36	12
Miscellaneous, Taxes and Receipts.....	37	16	46	100	4	4	7	4
	58	18	24	100	74	45	44	59
GROUP II (Chiefly Taxes on Business and Scarcity Value)—								
Corporation Taxes.....	68	32	—	100	15	14	—	11
Company Fees, Licences, etc.....	11	39	50	100	—	3	3	2
Public Domain.....	10	90	—	100	—	9	—	2
Business Property Taxes.....	—	—	100	100	—	—	5	1
Property Taxes on Real Estate.....	—	2	98	100	—	1	47	15
	25	21	54	100	16	27	55	31
GROUP III (Progressive Taxes)—								
Personal Income Taxes.....	79	18	3	100	11	5	1	6
Succession Duties.....	—	100	—	100	—	15	—	4
	50	48	2	100	11	20	1	10
Dominion Subsidies to Provinces.....	—	—	—	—	—	8	—	—
Total.....	47	22	31	100	100	100	100	100

greatest increase in public responsibilities has occurred in the field of public welfare which has grown from virtual insignificance to where it absorbs almost 30 per cent of the total government expenditures. Although the provinces and municipalities are now receiving substantial financial aid from the Dominion for these services, they are still paying more than half the total cost.

The economic and social changes within the framework of the Canadian constitution have raised the provinces and the municipalities to a very important position in the public finance system—a position which they cannot efficiently occupy on the basis of their necessarily limited revenue sources. This situation is especially aggravated by the increasing load of deadweight debt, the interest charges on which now comprise one-fifth the aggregate municipal-provincial expenditures.

Reviewing the present division of revenues and responsibilities between the different levels of government, it is clear that certain taxes and functions are pre-eminently either national or local in nature, but that there are many which cannot be so simply and satisfactorily classified. Of Dominion revenues, customs and excise duties are not only essentially central government taxes, but they are the very essence of a central government. This is so generally recognized that it does not require development, other than to note the possibility of departing from the principle and thwarting the intention of this fundamental allocation of powers by devising protective forms of local taxation and expenditure.

Our historical and economic review has shown the extent to which Dominion tariff policy, Dominion railway policy, and other necessarily associated national policies have built up an interdependent economy. The whole nature of economic activity and structure of private enterprise in Canada have been moulded by these national policies, and, of particular concern to public finance policy, the localization of net income from national enterprises has been largely determined by them. Certain public finance implications follow as a natural consequence.

The Dominion, by its large-scale intervention in the economic life of the country, and as a corollary of its conscious policies of selected stimuli, protection, and control, has unconsciously committed itself to many responsibilities for the maintenance of economic welfare. On the other hand, it has created a claim for itself to tax whatever surplus incomes and fortunes are accumulated within the framework of its policies.

These implications, as noted in our historical section, have not been generally recognized, and a fortuitous sequence of events concealed the necessity for recognizing them until recent years. We have noted how the Dominion, faced successively with the emergencies of war, the financial débâcle of its developmental program, and depression, turned to an *ad hoc* and somewhat indiscriminate imposition of taxes throughout nearly the whole field, and how it also assumed, in a tentative, inefficient manner, some of the responsibility for developmental programs and unemployment and drought relief which overwhelmed the provincial and local governments. At no time has the situation been reviewed and realistically faced; as a result the Dominion system includes neither the direct responsibility for maintaining certain minimum standards of governmental services, nor the undisputed control of the chief instruments of taxation of national net income that one might expect as an essential corollary of its responsibilities, and of the type of economy which has developed under its guidance. Instead, the Dominion has added to its basic customs and excise revenue sources a uniquely high sales tax, heavy corporation taxation and a personal income tax that rises steeply in the upper brackets.

As a result of this undirected growth the Dominion's public finance system is open to criticism both for what it includes and what it omits. Its taxation system is not adjusted to the national net income and under the present division of revenue powers cannot be so adjusted. Even the personal income tax, producing 11 per cent of the Dominion revenue and 5 per cent of total provincial revenues, takes widely varying proportions of equal incomes from residents of different provinces. The corporate income tax (which provinces also impose to varying degrees) is a flat-rate levy regardless of the income of the corporate shareholder and owner, and as such violates our generally accepted canons of equitable taxation. The remaining Dominion taxes—three-quarters of the total—have no direct (although in cases they may have an indirect) relationship to net income, considered from either an income class or regional point of view.

The total revenues of provincial governments are about half those of the Dominion; total municipal revenues are about two-thirds those of the Dominion. But while municipal revenue is largely concentrated on real property taxation, provincial revenues come from widely diversified sources. Of

first importance to provincial governments are consumption taxes, chiefly automobile (including gasoline) and liquor levies, accounting for nearly half the provincial revenues before subsidies. Taxes on business (including public domain revenues, which are, broadly speaking, alternatives of fundamentally the same character) make up a little more than a quarter of the total; taxes on income and inheritances, a little less than a quarter. The importance of the post-War development of provincial consumption taxes has been discussed in our historical review, but, although they now bulk largest in dollars and cents and have played a significant part in the shift in the balance of Dominion-provincial power, provincial business taxation, income taxation, and succession duties are perhaps of more particular concern for the present discussion. We have noted how the hard-pressed provinces branched out into new fields of taxation, and the cumbersome methods to which jurisdiction limitations compelled them to resort on occasion. Because of the very unequal distribution of corporate and entrepreneurial income and accumulated wealth throughout the country (partly as a result of the operation of national policies), this particular tax basis varies widely between provinces and has little relation to individual provincial responsibilities. It is in the employment of these forms of taxation that the greatest variations exist between provinces (and, of course, the greatest variations in incidence on individuals); vigorous application of these taxes in Ontario during a period of business recovery yielded the province a handsome surplus; no conceivable vigour of application could meet the western situation; reluctance to increase these forms of taxes left Quebec, and to a lesser extent the Maritimes, unable to balance their budgets.

4. PROVINCIAL FINANCES

In the following review of the financial position of the individual provinces per capita figures of revenue and expenditure have been used in order to facilitate comparisons. These figures must be considered in relation to the provincial income and particularly to the taxable surplus income, and also to the amount of services supplied through community agencies rather than privately, and to other special circumstances which may make direct comparison between two provinces misleading. In order to give for each province as accurate and comprehensive a picture of the financial position as possible, provincial and municipal revenues and expenditures have been combined. This is particularly necessary if comparisons are to be made between provinces, owing to the great variations in the division of responsibility for such functions as education, welfare, and highway maintenance. The proportion of the total cost of each of these services borne by the provincial government varies widely both as between provinces and in any one province as between periods. In all cases, although most notably in highway and relief expenditures, there has been a trend to assumption of an increasing share of the cost and increasing responsibility for administration by the provincial government.

All revenues and expenditures need not be discussed in the same detail in every province, and attention has been chiefly directed to those features which show significant variations between provinces and have a special bearing on Dominion-provincial relations and those which are of particular importance to the individual provincial fiscal system and economy. The major functions of education and public welfare (other than relief) which account for 35 per cent of provincial and municipal expenditures, are discussed together since they normally have similar characteristics. Relief expenditures in each province during recent years have been discussed in some detail in Chapter VI.

PRINCE EDWARD ISLAND

TABLE 87.—REVENUES ON CURRENT ACCOUNT—PER CAPITA, 1937

	Provincial and Municipal				Provincial		Municipal	
	\$ Per Capita		Percentage of Total Revenue		\$ Per Capita		\$ Per Capita	
	P.E.I.	All Prov.	P.E.I.	All Prov.	P.E.I.	All Prov.	P.E.I.	All Prov.
Real Property Taxes.....	4.43	22.60	20	45	1.13	0.53	3.30	22.07
Gasoline Taxes and Motor Vehicle Licences.....	4.45	5.84	20	12	4.45	5.84	—	—
Public Domain.....	—	1.90	—	4	—	1.90	—	—
Liquor Control.....	0.43	2.68	2	5	0.43	2.68	—	—
Miscellaneous Taxes, Licences, Fees, etc.....	3.14	6.85	14	15	1.36	1.64	1.78	5.20
Sub-Total.....	12.45	39.87	56	81	7.37	12.59	5.08	27.27
Sales Taxes.....	—	0.57	—	1	—	0.17	—	0.40
Corporation Taxes.....	1.77	3.06	8	6	1.77	3.06	—	—
Income Taxes on Persons.....	0.37	1.24	2	2	0.37	1.07	—	0.17
Succession Duties.....	0.48	3.22	2	6	0.48	3.22	—	—
Total Revenue from Provincial Sources.....	15.07	47.96	68	96	9.99	20.11	5.08	27.84
Federal Subsidies.....	7.06	1.91	32	4	7.06	1.91	—	—
TOTAL.....	22.13	49.87	100	100	17.05	22.02	5.08	27.84

Revenue System

Statistical comparisons between a unit with a total population of about one-tenth that of the Toronto metropolitan area and, say, the Province of Ontario are of little value or significance. For many purposes Prince Edward Island must be considered quite separately. But if a comparison is to be made with other provinces, the most striking feature of Prince Edward Island's provincial and municipal revenue system is the relatively large amount derived from federal subsidies—more than three times the per capita average for all provinces. Total provincial and municipal revenues from within the Province, on the other hand, are only one-third as much as the per capita average for all provinces, and not one of the chief taxes or groups of taxes is up to the average. There are, of course, special circumstances which account for this and such a comparison in itself cannot be taken as evidence that Prince Edward Island is under-taxed. The subsistence nature of the economy, the low average net value of agricultural production, and the lack of urbanization are reflected in a total real property tax yield which is only one-fifth the Canadian per capita average. The Province's lack of any public domain is responsible, of course,

for the absence of revenue from that source, and the Provincial Government's liquor control policy yields only a small fraction of the average receipts in other provinces. The absence of any notable concentration of corporate or personal income and wealth in the Island makes it impossible to secure a substantial yield from income taxes and succession duties, although special inducements have been granted companies to incorporate within the jurisdiction of the Island Government.

Not only is the revenue system affected by the lack of urban, industrial or individual concentrations of wealth in the Island economy, but also by the relatively low average income (scarcely more than one-half the Canadian average) which leaves little margin available for general consumption taxation. In spite of the fact that Prince Edward Island is the most perfect geographical entity of any Canadian province, it does not form a satisfactory unit from the point of view of public finance, and particularly for raising revenue. The manifest inability of a small agricultural economy, possessing no taxable surplus, to raise revenues and to finance services on the same scale as in the rest of Canada was recognized from the first in the special debt allowance, and subsidy in lieu of land, pro-

vided when Prince Edward Island entered Confederation. Much of Prince Edward Island's financial history since then has been one of subsidy claims and adjustments, and special increases in 1887, 1901, 1911, and 1935 maintained the subsidy as much the most important source of revenue.

As a result of the relatively large proportion of the revenue provided by the fixed subsidy and of the small proportion derived from such normally fluctuating sources as public domain, liquor control and progressive taxation, the Island Government's revenues are exceptionally stable but also inelastic.

TABLE 88.—EXPENDITURES ON CURRENT ACCOUNT—PER CAPITA, 1937

	Provincial and Municipal				Provincial		Municipal	
	\$ Per Capita		Percentage of Total Expenditure		\$ Per Capita		\$ Per Capita	
	P.E.I.	All Prov.	P.E.I.	All Prov.	P.E.I.	All Prov.	P.E.I.	All Prov.
Net Debt Charges.....	3.61	9.52	17	20	2.38	4.59	1.23	4.94
Public Welfare—								
Relief.....	0.84	5.45	4	11	0.52	3.86	0.32	1.59
Other.....	2.96	7.26	14	15	2.74	4.05	0.22	3.21
Education.....	5.90	9.78	28	20	3.76	2.89	2.15	6.89
Agriculture and Public Domain.....	0.49	1.86	2	4	0.50	1.86	—	—
Transportation.....	4.35	5.03	20	10	3.60	2.27	0.75	2.75
General Government and Miscellaneous.....	3.17	9.80	15	20	2.26	3.77	0.89	6.03
Total.....	21.32	48.70	100	100	15.76	23.29	5.56	25.41
Per Capita Provincial Income, \$.....	194	345	—	—	—	—	—	—
Per Capita Outstanding Debt, \$.....	92	291	—	—	64	177	28	115
Percentage of Current Expenditures to Provincial Income.....	11	14	—	—	8	7	3	7
Percentage of Outstanding Debt to Provincial Income.....	47	84	—	—	33	51	14	33

Expenditures

In keeping with the rigid and limited character of governmental revenues, provincial and municipal governments have performed their functions with great frugality and economy. The small area and population of the Province have made it possible to dispense with an extensive municipal organization, but, on the other hand, there are certain basic essentials of provincial government which must be provided. Even when the overhead costs of these are kept at the possible minimum level they are uncontrollable and relatively high in relation to the small population. All the functions of government are provided for at substantially lower per capita costs than in other provinces, in part because these functions are much simpler in such a small unit, in part because smaller cash incomes can be paid in a community which largely lives on its own produce, and in part because the Government cannot afford to pay more.

Debt charges have in the past been held at a relatively low figure (about one-third of the Canadian average per capita) because the Province has not had to provide expensive transportation and frontier developmental facilities.* But this position has been somewhat altered by the Province's highway and relief work program in recent years, and net interest charges have more than doubled during the last decade. Borrowing has been done, however, at relatively advantageous rates, and the technical position of the provincial debt is exceptionally strong. There are no bonds payable in other than Canadian currency now outstanding; maturities are evenly spaced; and the sinking fund is strong.

Expenditures on education are some 40 per cent below the national average per capita and expenditures on public welfare (other than relief) 60 per cent less. It is true that a less varied and high

* It may, however, be noted that the Province became bankrupt through railway expansion prior to its entry into Confederation.

degree of specialization is necessary; that necessary physical plant is cheaper; that lower costs of living permit payment of lower salaries; and that family solidarity and a relatively high degree of self-sufficiency bear many burdens which are transferred to the state in other provinces, but in spite of all these factors, it is clear that standards are inadequate and below the average in many cases.

Direct relief expenditures have been kept to relatively negligible amounts, but the provincial government's public works program has been carried out on a large scale and has been responsible for aggregate expenditures on relief, relief works and other public works equal to the same percentage of the provincial income as similar expenditures in Ontario.

Transportation expenditures are closer to the national average than expenditures for most other services, and efforts to encourage the tourist trade may increase them. Expenditures on agriculture and development of other resources are low, in part owing to the lack of any provincial public domain, but this may be one of the fields in which enforced economy has been costly in view of the necessity of utilizing and co-ordinating the Island's limited resources to the maximum possible advantage.

Summary

With federal subsidies providing for approximately one-third of total provincial-municipal expenditures, and with some reserve of taxation (although in view of the general economic position of the Island's agricultural industry, no great reserve), it should be possible to maintain and gradually to improve services under the present system. Expenditures have been economically administered and the Island's credit and prospects of financial stability are good. On the other hand, there is little prospect under the present system of the Island Government being able to raise sufficient taxation from the sources open to them to bring the standards of governmental services to real equality with those in the rest of the country. This is a factor of growing importance owing to the cessation of the emigration which formerly absorbed the Island's natural increase of population. To provide for this population increase it would appear necessary either to foster some intensive domestic development, for which no economic base is at present evident, or to equip potential emigrants with at least as good training and education as possessed by other Canadians.

NOVA SCOTIA

TABLE 89.—REVENUES ON CURRENT ACCOUNT—PER CAPITA, 1937

	Provincial and Municipal				Provincial		Municipal	
	\$ Per Capita		Percentage of Total Revenue		\$ Per Capita		\$ Per Capita	
	N.S.	All Prov.	N.S.	All Prov.	N.S.	All Prov.	N.S.	All Prov.
Real Property Taxes.....	13.02	22.60	37	45	0.88	0.53	12.14	22.07
Gasoline Taxes and Motor Vehicle Licences.....	6.24	5.84	18	12	6.24	5.84	—	—
Public Domain.....	1.54	1.90	4	4	1.54	1.90	—	—
Liquor Control.....	2.66	2.68	7	5	2.66	2.68	—	—
Miscellaneous Taxes, Licences, Fees, etc.....	5.43	6.85	15	15	0.73	1.64	4.70	5.20
Sub-Total.....	28.89	39.87	81	81	12.05	12.59	16.84	27.27
Sales Taxes.....	—	0.57	—	1	—	0.17	—	0.40
Corporation Taxes.....	2.07	3.06	6	6	2.07	3.06	—	—
Income Taxes on Persons.....	0.09	1.24	0	2	—	1.07	0.09	0.17
Succession Duties.....	0.93	3.22	3	6	0.93	3.22	—	—
Total Revenue from Provincial Sources.....	31.98	47.96	90	96	15.05	20.11	16.93	27.84
Federal Subsidies.....	3.60	1.91	10	4	3.60	1.91	—	—
TOTAL.....	35.58	49.87	100	100	18.65	22.02	16.93	27.84

Revenue System

Nova Scotia's revenues per capita are about two-thirds the Canadian average, provincial revenues being 85 per cent and municipal revenues only 60 per cent of the average. The most striking features in comparison with most other provinces are the low returns from real property taxation, and the relatively high proportion of total revenues provided by the federal subsidy. The long history of adverse economic conditions, the depletion of some of the best resources, the prevalence of small-scale subsistence industry, and the vulnerability of Nova Scotia's specialized industries are responsible for the low taxable capacity. Government efforts to raise revenues without further reducing the provincial income are particularly difficult since the normal method—progressive taxation—would not be productive on an important scale in Nova Scotia. As a second best choice Nova Scotia has turned to consumption taxation of selected commodities. Liquor and gasoline taxation make up 25 per cent of the total revenue as compared with 17 per cent in all provinces. Public domain revenues, of which the great bulk are coal royalties, are of rather

special character since a large proportion of the production is made possible only through Dominion subsidies and protection. Consequently, the provincial revenues from its public domain are in a sense paid by the Dominion Government. The revenue base is thus narrow and limited. Revenues from public domain must be related to the extent to which the Dominion is prepared to subsidize the mining industry. The gasoline tax rate is limited by the desire to attract tourists from the United States, although it should be noted that a high rate in Nova Scotia is less oppressive than in a province of much greater distances such as Saskatchewan. Liquor taxation, of course, is shared with the Dominion, and provincial revenues from that source will be affected by Dominion policy. Income tax and succession duty yields must inevitably be low unless relatively high taxation is imposed on quite small incomes. The marginal nature of the economy makes general consumption taxation, including property and sales taxes, undesirable. There is evidently great temptation to turn to corporation taxes and constant pressure to demand increased federal subsidies.

TABLE 90.—EXPENDITURES ON CURRENT ACCOUNT—PER CAPITA, 1937

	Provincial and Municipal				Provincial		Municipal	
	\$ Per Capita		Percentage of Total Expenditure		\$ Per Capita		\$ Per Capita	
	N.S.	All Prov.	N.S.	All Prov.	N.S.	All Prov.	N.S.	All Prov.
Net Debt Charges.....	7.15	9.52	21	20	4.83	4.59	2.32	4.94
Public Welfare—								
Relief.....	1.15	5.45	3	11	0.83	3.86	0.32	1.59
Other.....	6.30	7.26	19	15	3.24	4.05	3.06	3.21
Education.....	7.78	9.78	23	20	2.37	2.89	5.41	6.89
Agriculture and Public Domain.....	1.06	1.86	3	4	1.06	1.86	—	—
Transportation.....	4.65	5.03	14	10	3.75	2.27	0.90	2.75
General Government and Miscellaneous.....	5.66	9.80	17	20	2.01	3.77	3.65	6.33
TOTAL.....	33.75	48.70	100	100	18.09	23.29	15.66	25.41
Per Capita Provincial Income, \$.....	290	345	—	—	—	—	—	—
Per Capita Outstanding Debt, \$.....	215	291	—	—	172	177	44	115
Percentage of Current Expenditure to Provincial Income.....	12	14	—	—	6	7	5	7
Percentage of Outstanding Debt to Provincial Income.....	74	84	—	—	59	51	15	33

Expenditures

Although the provincial government's net debt charges are at the same per capita level as in other provinces (and a higher proportion of provincial government revenues), municipal charges are only half the per capita average, making the total debt burden approximately three-quarters of the Canadian average. (In 1937 provincial income was 84 per cent of the Canadian per capita average.) Outstanding provincial debt doubled during the thirties, three-quarters of the increase being due to highway expenditures, and the balance to current deficits, including direct relief. The debt maturities are fairly evenly spaced up to 1952. Nearly half the debt is optionally payable in other than Canadian currency and is of relatively long-term and high-coupon rates. Recent borrowing at favourable rates has brought the average coupon rate below 4 per cent, but no refunding of the major portion of the high coupon debt will be possible for some time.

General government expenditures are less than 60 per cent of the national per capita average, and detailed comparisons indicate very frugal administration. On the other hand, it has been argued that a better paid civil service would make for long-run economy.

On education and public welfare (excluding relief) Nova Scotia is now spending proportionately more of total municipal-provincial revenues than other provinces, but still some 20 per cent less than the national per capita average. There has been notable improvement in these services since the granting of the Duncan and White Commissions' awards, and to some extent the lower than average level of expenditure is justified by lower costs and does not indicate inferior standards. Nevertheless some of the needs are greater—the high proportion of the population in the older age groups, the presence of some specially destitute rural areas, and the necessity of maintaining mobility of population, and of equipping emigrants with competitive techniques, all create special demands. The full importance of altered circumstances and competitive conditions was perhaps not appreciated for some time owing to the reserve accumulated from Golden Age days of an initially well-equipped and administered educational system.

The relief problem has been largely met in recent years by the provincial government's relief works and highways programs, and by the Dominion government's assistance to the coal and steel industry. The provincial government found the depression a favourable time at which to modernize its highway system with the advantages of cheap money and of using labour which would otherwise have been unemployed. It was hoped that this program would strengthen the economy by attracting tourist trade and lowering transportation charges, but it is still too early to determine whether the investment will prove self-supporting and what the employment situation will be when the program is terminated.

Transportation expenditures have absorbed a somewhat higher proportion of government revenues than average, but it is hoped that the new highway system will reduce maintenance costs. These expenditures afford a good example of the variation in provincial-municipal division of costs of various services throughout Canada. In Nova Scotia the provincial government supplies more than four-fifths of the total current expenditures on streets and roads; in the rest of Canada provincial governments supply less than half. Expenditures on public domain are small and have been kept fairly constant. Expenditures on agriculture have increased but those on forests have fallen perhaps below the minimum necessary in a region where conservation and protection are imperative.

Summary

Nova Scotia's provincial income reflects the long struggle of the region with serious economic disabilities. The relatively low and variable cash proportion of the income, and the fact that an important amount of the surplus income and wealth is drained off to Central Canada impose limitations on the tax system and at the same time create special demands for expenditures. The current effort to strengthen the economy by large scale capital expenditures has added substantial fixed charges, and the debt structure is such that there is little prospect of reduction in existing charges through normal refunding operations. Under the present system chronic pressure for increased federal subsidies and provincial services of less than average standards would appear inevitable.

NEW BRUNSWICK

TABLE 91.—REVENUES ON CURRENT ACCOUNT—PER CAPITA, 1937

	Provincial and Municipal				Provincial		Municipal	
	\$ Per Capita		Percentage of Total Revenue		\$ Per Capita		\$ Per Capita	
	N.B.	All Prov.	N.B.	All Prov.	N.B.	All Prov.	N.B.	All Prov.
Real Property Taxes.....	10.11	22.60	31	45	0.26	0.53	9.85	22.07
Gasoline Taxes and Motor Vehicle Licences.....	5.72	5.84	18	12	5.72	5.84	—	—
Public Domain.....	2.47	1.90	8	4	2.47	1.90	—	—
Liquor Control.....	2.51	2.68	8	5	2.51	2.68	—	—
Miscellaneous Taxes, Licences, Fees, etc.....	5.37	6.85	16	15	0.55	1.64	4.82	5.20
Sub-Total.....	26.18	39.87	81	81	11.51	12.59	14.67	27.27
Sales Taxes.....	—	0.57	—	1	—	0.17	—	0.40
Corporation Taxes.....	1.18	3.06	4	6	1.18	3.06	—	—
Income Taxes on Persons.....	0.29	1.24	1	2	—	1.07	0.29	0.17
Succession Duties.....	0.90	3.22	3	6	0.90	3.22	—	—
Total Revenue from Provincial Sources.....	28.55	47.06	89	96	13.59	20.11	14.96	27.84
Federal Subsidies.....	3.56	1.91	11	4	3.56	1.91	—	—
TOTAL.....	32.11	49.87	100	100	17.15	22.02	14.96	27.84

Revenue System

Total provincial-municipal revenues in New Brunswick are only two-thirds the national per capita average and, excluding Prince Edward Island, are the lowest in Canada. As in the other Maritime Provinces real property taxation is much below the average (in New Brunswick less than half the per capita average) and progressive taxation yields are negligible. Reliance has consequently been placed on selected consumption taxation (gasoline and liquor), public domain revenues, and on federal subsidies. The latter make up 11 per cent of total provincial-municipal revenues in New Brunswick as compared with the national average of 4 per cent. The nature of the provincial economy and of the provincial income (which is only 70 per cent of the national average) has been previously discussed in Chapter VII and accounts for the limited base of the revenue system. Where so many of the resources are marginal and so many of the incomes at bare subsistence levels, increased taxation on costs would submerge an important portion of the economy. In such a region there is little accumulated surplus wealth or

surplus income. It is not clear, however, that the Province's efforts to tax what surplus income does exist have been as vigorous as possible; the income tax has been left to municipalities and succession duty rates are on balance lower than the average. The municipal income tax (with the exception of the Saint John income surtax) is levied on a frequently arbitrary assessment at the local real property tax rate with exemptions varying according to local conditions. It has become in fact a combination of a small poll tax and a rough approximation of a property tax but even when combined with real property taxation the total yield is less than half the Canadian per capita average. It is in this deficiency that much of New Brunswick's financial difficulty may lie. Municipalities cannot carry the same share of education, welfare and highway expenditures as they do in other provinces and the provincial government lacks the financial resources and tax basis to make good the difference. Nevertheless it is scarcely necessary to add that a doubling of real property taxation in New Brunswick is impracticable and even any substantial increase would require such a wholesale adjustment of rents and wages and lead

to such an increased burden on the costs of many marginal enterprises that it would seriously damage provincial income and taxable capacity. The public domain revenues are above the average but are very dependent on the fluctuating fortunes of the lumbering industry, royalties and stumpage taxes, for example rising six-fold from 1933 to 1937. However, the relative decline in the competitive

power of many of New Brunswick's natural resources limits their revenue possibilities. Corporation taxes have recently been extended and increased and the yield has been doubled, but it is evident that unless discriminatory forms of corporation taxation on extra-provincial companies are resorted to this source can never be a major revenue producer.

TABLE 92.—EXPENDITURES ON CURRENT ACCOUNT—PER CAPITA, 1937

	Provincial and Municipal				Provincial		Municipal	
	\$ Per Capita		Percentage of Total Expenditure		\$ Per Capita		\$ Per Capita	
	N.B.	All Prov.	N.B.	All Prov.	N.B.	All Prov.	N.B.	All Prov.
Net Debt Charges.....	8.80	9.52	30	20	6.33	4.59	2.47	4.94
Public Welfare—								
Relief.....	0.59	5.45	2	11	0.42	3.86	0.17	1.59
Other.....	4.42	7.26	15	15	2.32	4.05	2.10	3.21
Education.....	6.08	9.78	21	20	1.66	2.89	4.42	6.89
Agriculture and Public Domain.....	1.49	1.86	5	4	1.49	1.86	—	—
Transportation.....	3.67	5.03	13	10	2.62	2.27	1.05	2.75
General Government and Miscellaneous.....	4.13	9.80	14	20	1.49	3.77	2.64	6.03
TOTAL.....	29.18	48.70	100	100	16.33	23.29	12.85	25.41
Per Capita Provincial Income, \$.....	239	345	—	—	—	—	—	—
Per Capita Outstanding Debt, \$.....	233	291	—	—	186	177	46	115
Percentage of Current Expenditure to Provincial Income.....	12	14	—	—	7	7	5	7
Percentage of Outstanding Debt to Provincial Income.....	97	84	—	—	78	51	19	33

Expenditures

The foregoing table does not show the marked increase in net debt charges in the most recent years. But, even in 1937, in spite of municipal debt charges which were only half the Canadian average, total provincial and municipal debt charges almost equalled the national average and absorbed 30 per cent of revenue as compared with 20 per cent for all of Canada. This is the highest proportion in Canada by quite a margin. It is the heritage of public works expenditures and other governmental efforts undertaken in the past to aid and strengthen the economy but which, in the face of the serious economic disabilities under which New Brunswick laboured, failed to stimulate income and taxable capacity significantly. The rate of increase in the last two years has been alarming, and in view of the already excessive amount of deadweight debt

burden, the Province's credit is now seriously threatened. Nearly one-half the provincial government's debt is optionally payable in currencies other than Canadian and four-fifths of its bonds bearing 4½ per cent and higher coupons will not mature for ten years or longer. The result is that there is little prospect of saving from refunding in the near future.

General government expenditures, particularly on the administration of justice, were cut substantially during the depression and are the lowest per capita in the Dominion. There is some danger that this economy has been purchased at the expense of efficient administration. On education and public welfare New Brunswick spends only about 60 per cent of the national per capita average. Nevertheless as a consequence of the poverty which restricts New Brunswick's revenues the need for expenditures

on the social services in general is greater than the average. New Brunswick has the highest proportion in Canada of very old and very young non-workers to its total population and has also a number of seriously depressed areas in which living standards have been reduced to very bare subsistence levels. Unemployment, as we have noted, has not recently been an important provincial problem but widespread and chronic poverty is a most serious one. Expenditures on welfare and education in relation to the needs are very low; even after adjustment for the lower costs resulting from less urbanization and lower salary scales, they are far below the Canadian average.

As in the other Maritime Provinces the self-subsistence nature of the economy reduced the necessity for extensive government relief but the most important factor in the employment situation in New Brunswick was the Government's extensive highway program. After severe curtailment of all capital expenditures in the depths of the depression a highway construction program was launched, and in recent years has been carried out on an unprecedented scale, directly contributing some 10 per cent of the total provincial income. Directly and indirectly this has met the unemployment problem for the time being, but has created fiscal problems of the first magnitude for the Government. It would seem clear that New Brunswick's program was initially a well-timed one and provided necessary and productive public works on very favourable terms, but it is also clear that the policy cannot be continued on anything approaching the same scale. It is still too early to weigh the costs and profits of the modern highway system which is being constructed and to determine whether it would be advantageous to fill in the network with secondary roads on an equally ambitious scale, but it must be recognized that substantial reduction of the Government's capital program will (unless some alternative stimulus appears) revive unemployment and relief problems.

Current expenditures on domain and transportation are somewhat larger in proportion to revenue, although somewhat less in dollars per capita, than the Canadian average. Highway maintenance expenditures have dropped and may drop further as a result of the improved roads now being constructed; public domain expenditures, however, may be too low to conserve and develop resources efficiently.

Summary

The Government's present highway program is only the most recent of a series of efforts to improve transportation facilities (which, owing in part to the large number of bridges in the "best watered country in the world," have always been costly) and encourage economic development. In the past the generally unfavourable trend of economic events has defeated these projects and has left the Province with both a costly burden of deadweight debt and inflated current expenditures. At the same time the economic difficulties of the Province have increased the need for positive action in the form of better education, research and development, and for defensive action through provision of public health and social service facilities. The low taxable capacity of the Province combined with reluctance to resort to direct taxation have made it impossible to raise sufficient revenues to finance both a positive developmental program and to provide educational, social service and public health services up to average Canadian standards. Debt charges and highway maintenance alone now take 55 per cent of provincial government expenditures as compared with the Canadian average of 30 per cent. Even substantial increases in provincial taxation would still leave New Brunswick hard pressed to carry her present burdens and forced to plead for increased federal subsidies as the chief hope for expanding those services which are at present much below the Canadian average.

QUEBEC

TABLE 93.—REVENUES ON CURRENT ACCOUNT—PER CAPITA, 1937

	Provincial and Municipal				Provincial		Municipal	
	\$ Per Capita		Percentage of Total Revenue		\$ Per Capita		\$ Per Capita	
	Que.	All Prov.	Que.	All Prov.	Que.	All Prov.	Que.	All Prov.
Real Property Taxes.....	19.28	22.60	43	45	—	0.53	10.28	22.07
Gasoline, Taxes and Motor Vehicle Licences.....	4.62	5.84	10	12	4.62	5.84	—	—
Public Domain.....	2.03	1.90	5	4	2.03	1.90	—	—
Liquor Control.....	2.25	2.68	5	5	2.25	2.68	—	—
Miscellaneous Taxes, Licences, Fees, etc.....	7.42	6.85	16	15	1.97	1.64	5.45	5.20
Sub-Total.....	35.60	39.87	79	81	10.87	12.59	24.73	27.27
Sales Taxes.....	1.41	0.57	3	1	—	0.17	1.41	0.40
Corporation Taxes.....	3.08	3.06	7	6	3.08	3.06	—	—
Income Taxes on Persons.....	0.54	1.24	1	2	—	1.07	0.54	0.17
Succession Duties.....	3.57	3.22	8	6	3.57	3.22	—	—
Total Revenue from Provincial Sources.....	44.20	47.96	98	96	17.52	20.11	26.68	27.84
Federal Subsidies.....	0.83	1.91	2	4	0.83	1.91	—	—
TOTAL.....	45.03	49.87	100	100	18.35	22.02	26.68	27.84

Revenue System

The Quebec revenue system as a whole conforms closely to the statistical average pattern, the chief differences being the exercise of income and sales tax powers by the municipalities rather than by the provincial government and the somewhat higher proportion of joint provincial-municipal revenues raised by municipalities. The most notable factor in relation to provincial income is the absence of highly developed progressive taxation. Per capita income in Quebec is somewhat less than average, but the extremes of distribution of income are far greater than average. The aggregate provincial income is made up of a small group of very high incomes and a large group of very low incomes. Nevertheless the personal income tax has been levied only municipally in the Montreal metropolitan area, and for the decade ending 1937 succession duty collections just equalled the national per capita average. To some extent this is explained by the historical fact that Quebec's finances were formerly in a uniquely strong position. Public domain revenues and liquor control profits were high and other taxation was unnecessary on the same scale

as in the other provinces. But the fall in liquor profits from a peak of \$12.3 million to a low of \$2.4 million and of domain revenues from \$7.4 million to \$2.9 million during the depression completely altered the revenue picture. Provincial efforts to increase revenues were hampered, however, by the situation of the equally hard-pressed municipalities.

The municipal and real property tax situation was particularly complicated by the unique role which the Church plays in Quebec. Many functions, particularly in the field of public welfare and education, which are carried out by the local or provincial governments in other provinces are supported by the Church in Quebec. Although the personnel engaged on these services serve for merely nominal pay, there are substantial and unavoidable overhead costs which in the last analysis must be borne by the same incomes that support provincial and municipal taxation. As a result the Quebec taxpayer contributes more for services which in other provinces are largely supplied by the state than is evident from public finance statistics. These costs affect real estate in particular, both directly and through

the exemption from taxation of the major portion of religious property. In part as a result of this situation some municipalities have turned to income and sales taxes, and to a number of licences and fees which are in effect corporation taxes in some cases, and this development has in turn restricted provincial freedom of action. Nevertheless the

provincial government, in its search for additional revenues, has sharply increased corporation taxes.

The federal subsidy in the Quebec revenue system plays a relatively insignificant role, providing less than 2 per cent of provincial-municipal revenues. It is also worth noting the provincial subsidies to municipalities are only one-fifth those in Ontario.¹⁶

TABLE 94.—EXPENDITURES ON CURRENT ACCOUNT—PER CAPITA, 1937

	Provincial and Municipal				Provincial		Municipal	
	\$ Per Capita		Percentage of Total Expenditure		\$ Per Capita		\$ Per Capita	
	Que.	All Prov.	Que.	All Prov.	Que.	All Prov.	Que.	All Prov.
Net Debt Charges.....	9.44	9.52	20	20	2.19	4.59	7.25	4.94
Public Welfare—								
Relief.....	6.65	5.45	14	11	4.15	3.86	2.50	1.59
Other ^(a)	5.56	7.26	12	15	3.37	4.05	2.19	3.21
Education ^(a)	7.24	9.78	15	20	1.97	2.89	5.27	6.89
Agriculture and Public Domain.....	3.49	1.86	7	4	3.49	1.86	—	—
Transportation.....	4.87	5.03	10	10	2.37	2.27	2.50	2.75
General Government and Miscellaneous.....	10.10	9.80	22	20	3.98	3.77	6.12	6.03
TOTAL.....	47.35	48.70	100	100	21.52	23.29	25.83	25.41
Per Capita Provincial Income, \$.....	299	345	—	—	—	—	—	—
Per Capita Outstanding Debt, \$.....	242	291	—	—	91	177	151	115
Percentage of Current Expenditure to Provincial Income.....	16	14	—	—	7	7	9	7
Percentage of Outstanding Debt to Provincial Income.....	81	84	—	—	30	51	51	33

^(a)See discussion in the text of qualifications necessary in comparing reported expenditures on these services in Quebec with expenditures in other provinces.

Expenditures

The net debt charges of the provincial government were still only half the national per capita average in 1937, but municipal debt charges brought the total to the average. The debt charges of religious institutions performing public services are unknown. Provincial net debt charges rose from the extraordinary low figure of 5 per cent of provincial revenue in 1930 (Canadian average then 17 per cent) to 12 per cent in 1937. Municipal debt charges, which have consistently been above the Canadian average as a percentage of revenue, increased further to 27 per cent of municipal revenues. With municipal debt charges per capita some 50 per cent above the Canadian average the rapid increase in provincial debt charges in recent years has been particularly serious. Provincial debt

approximately tripled between 1929 and 1937. A little more than one-third of the increase was represented by tangible assets (chiefly highways) and the balance by relief, poor loans, and current deficits. The previous high credit standing of the provincial government permitted borrowing on favourable terms and, owing in part to this and in part to resort to shorter term securities, the average coupon rate on outstanding bonds was reduced from 4½ per cent in 1929 to 3½ per cent in 1937. Virtually all the borrowing during this period was in Canadian currency. However, the relatively large amount of short-term securities outstanding leaves Quebec in a potentially vulnerable position if the Province's credit rating should weaken or if interest rates should rise. Municipal debts rose by one-third during the same period while in all other provinces they declined or rose only slightly. The greatest

¹⁶Book III, Table 61.

proportion of increase was in the Montreal metropolitan area but "other urban" and "rural" municipalities also showed important increases. Some advantage has been gained from refunding at lower interest rates but the deadweight burden is still increasing as municipal budgets as a whole are not yet balanced.

General government expenditures are slightly more, both per capita and in proportion to total expenditures, for both provincial and municipal governments than in the rest of Canada and have been consistently so in the past. Education and public welfare (excluding relief) expenditures are lower than the Canadian average, partly because of the previously mentioned contribution of the Church. These have also been restricted by the growing pressure of deadweight debt charges and relief on municipal budgets. There are many special problems in connection with these services in Quebec which reduce the value of a statistical approach or comparison and make it impossible to assess relative standards. The Church has not only traditionally assumed a direct responsibility for education and public welfare to an important extent, but it has also thrown the full weight of its influence behind the enforcement of family responsibility for provision of these services with important effects on the residual burden on governments. Thus comparisons with expenditures in other provinces must take account of the large contribution made by the Church, and of the greater than average contribution made by the recipients themselves and their relatives, but no precise monetary estimate of this contribution is possible.¹⁷

The particularly acute relief situation in Quebec has been discussed in Chapters VI and VII. The problem centred largely on the huge pool of unemployed, mostly of unskilled labour, which gathered in the Montreal metropolitan area. Direct relief payments on a very large scale in Montreal, back-to-the-land resettlement and colonization programs and sporadic public works projects piled up provincial-municipal deficits at the rate of about \$20 million a year on current account, and were responsible for slightly more than one-half the \$310 million increase in provincial-municipal debt from 1929 to 1937 (most of the balance was incurred for highways).

Public domain and development expenditures in Quebec are much higher than average as might be expected in a province with the extensive natural resources and the regional economic problems of

Quebec.¹⁸ These problems are serious, and adequate conservation, development, and research are essential if the Quebec economy is to achieve a stable balance and income.

Highway maintenance expenditures in Quebec have in the past been above the average, and have to some extent been a corollary of low capital expenditures. It is expected that the recent large investment in improved highways will be reflected in lower maintenance charges but it is doubtful whether Quebec received the same value from its expenditures on highway projects launched as relief works as did the Maritimes, for example, since the projects do not appear to have been as well planned and economically executed.

Summary

The financial position of Quebec, long considered the fiscal Gibraltar of the Canadian provinces, deteriorated alarmingly during the depression. The very strong financial position of the provincial government at the beginning of the depression, purchased in part at the expense of the municipalities and institutions, long tended to conceal the real position and the full importance of the change in circumstances. Quebec, faced with the collapse of the very large sector of its economy which was dependent on world trade and with widespread distress in both depressed urban and rural areas, was forced to make large-scale expenditures for relief and to launch positive and constructive remedial policies at a time when a number of its chief revenues were dwindling rapidly.

Municipal and institutional finances were also under severe pressure and those units were incapable of assuming any greater burdens. The provincial revenue system proved to be a fair weather one only, yet efforts to broaden its base were hampered by the plight of the municipalities. Delay in facing the need for a complete overhaul of both provincial and municipal revenue systems in the light of the radical changes in economic circumstances which had occurred was responsible for piling up a heavy burden of deadweight debt. Quebec would appear still to have some latent reserves of credit and taxation but will require a fairly drastic reorganization of the provincial and municipal division of revenues and responsibilities, and a substantial broadening of the joint provincial-municipal tax basis to provide for the new level of expenditures and debt.

¹⁷ Appendix 5. *Esdras Minville, Labour Legislation and Social Services in the Province of Quebec*, pp. 47-49.

¹⁸ See Chapter VII.

ONTARIO

TABLE 95.—REVENUES ON CURRENT ACCOUNT—PER CAPITA, 1937

	Provincial and Municipal				Provincial		Municipal	
	\$ Per Capita		Percentage of Total Revenue		\$ Per Capita		\$ Per Capita	
	Ont.	All Prov.	Ont.	All Prov.	Ont.	All Prov.	Ont.	All Prov.
Real Property Taxes.....	29.10	22.60	51	45	0.06	0.53	29.04	22.07
Gasoline Taxes and Motor Vehicle Licences.....	7.12	5.84	12	12	7.12	5.84	—	—
Public Domain.....	1.44	1.90	2	4	1.44	1.90	—	—
Liquor Control.....	2.82	2.68	5	5	2.82	2.68	—	—
Miscellaneous Taxes, Licences, Fees, etc.....	6.18	6.85	11	15	1.50	1.64	4.68	5.20
Sub-Total.....	46.66	39.87	81	81	12.94	12.59	33.72	27.27
Sales Taxes.....	—	0.57	—	1	—	0.17	—	0.40
Corporation Taxes.....	2.80	3.06	5	6	2.80	3.06	—	—
Income Taxes on Persons.....	1.63	1.24	3	2	1.63	1.07	—	0.17
Succession Duties.....	5.45	3.22	10	6	5.45	3.22	—	—
Total Revenue from Provincial Sources.....	56.54	47.96	99	96	22.82	20.11	33.72	27.84
Federal Subsidies.....	0.79	1.91	1	4	0.79	1.91	—	—
TOTAL.....	57.33	49.87	100	100	23.61	22.02	33.72	27.84

Revenue System

The outstanding feature of the Ontario revenue system is the high yield, both proportionately and absolutely, of real property taxation. This particular source has long been the backbone of Ontario public finance as might be expected from the highly urbanized character of the economy. It is chiefly through real property taxation that Ontario governments have taken advantage of the wealth and income which natural advantages and national policies concentrate in Ontario. In addition, Ontario has been in a particularly favoured position to develop income taxes and succession duties to tap the same taxable surpluses. In the decade ending 1937 Ontario collected \$100 million of total succession duty collections of \$180 million in Canada. In 1937 succession duties and income taxes amounted to \$7 per capita, or nearly one-half the total revenue of the provincial government in Quebec, for example.

The other taxes are normally lower in rate but yield as much per capita as in the rest of Canada. Corporation taxes actually yield less per capita, in spite of the overwhelming concentration of corporations in Ontario, the generally strong financial

position of the provincial government having allowed it in the past to avoid carrying this particularly undesirable type of taxation to the extremes found necessary by most of the other provinces. The closely related public domain revenues are also less than average, the important mining industry yielding less than one-half a million a year in royalties and licences. This is particularly notable in view of the wasting character of that industry's assets, its high current rate of profits, the large public expenditures which were made to facilitate mining development, and the large public expenditures which will have to be made when the mines are exhausted. Ontario has already seen the virtual extinction of former flourishing industries based on natural resources, such as Ottawa Valley lumbering and Cobalt silver mining, and adequate conservation measures where these resources can be economically maintained, or financial preparation for necessary future adjustments where the resources are exhaustible would seem desirable.

The high level of property taxation has put Ontario municipalities on the whole in a comfortable financial position. In addition, the relatively

high yield of provincial taxation has enabled the provincial government to assist the municipalities. This position is in essence, of course, simply a reflection of the much higher average per capita income enjoyed in Ontario—in 1937, 43 per cent above the rest of Canada. But if national policies stimulate Ontario's income, national taxation takes a substantial amount of the cream, and Ontario's

taxation to a greater extent than in other provinces is affected by federal tax policy. In the field of progressive taxation, in particular, Ontario's action is restricted and future development will be largely determined by federal policy. In return, federal subsidies are relatively negligible—in 1937 they provided less than 1½ per cent of provincial-municipal revenues.

TABLE 96.—EXPENDITURES ON CURRENT ACCOUNT—PER CAPITA, 1937

	Provincial and Municipal				Provincial		Municipal	
	\$ Per Capita		Percentage of Total Expenditure		\$ Per Capita		\$ Per Capita	
	Ont.	All Prov.	Ont.	All Prov.	Ont.	All Prov.	Ont.	All Prov.
Net Debt Charges.....	9.46	9.52	18	20	4.99	4.59	4.47	4.94
Public Welfare—								
Relief.....	4.15	5.45	8	11	2.75	3.86	1.40	1.59
Other.....	8.63	7.26	17	15	4.55	4.05	4.08	3.21
Education.....	12.01	9.78	23	20	3.19	2.89	8.82	6.89
Agriculture and Public Domain.....	0.98	1.86	2	4	0.98	1.86	—	—
Transportation.....	5.76	5.03	11	10	2.11	2.27	3.65	2.75
General Government and Miscellaneous.....	10.69	9.80	21	20	4.00	3.77	6.69	6.03
TOTAL.....	51.68	48.70	100	100	22.57	23.29	29.11	25.41
Per Capita Provincial Income \$.....	430	345	—	—	—	—	—	—
Per Capita Outstanding Debts \$.....	338	291	—	—	218	177	121	115
Percentage of Current Expenditure to Provincial Income.....	12	14	—	—	5	7	7	7
Percentage of Outstanding Debts to Provincial Income.....	79	84	—	—	51	51	28	33

Expenditures

Nearly one-half the debt of the Ontario Provincial Government, largely that portion represented by the Ontario Hydro-Electric Power Commission, is directly self-supporting, and while gross interest payments in 1937 were \$33.2 million, net interest charges were only \$18.5 million. Total net debt charges of provincial and municipal governments are almost exactly the Canadian per capita average and have increased somewhat less than the average during the thirties, although the provincial government's net debt charges alone have approximately doubled. Municipal charges have actually decreased and consequently aggregate provincial-municipal charges increased only from \$30 million in 1930 to \$35 million in 1937. The coupon rate on the provincial government's debt is relatively high (4.3 per cent in 1937) as a result of heavy borrowings at

the high rates prevailing in the early twenties and again in the early thirties. However, \$100 million of the 4½ per cent and higher coupon rate debt matures in 1942 and 1943, and nearly two-thirds of this debt matures by 1950. Maturities are fairly evenly spread, as a result in part of a number of serial issues which make up 30 per cent of the outstanding debt, but sinking fund provisions for the balance of the debt are relatively small. Slightly more than one-half the debt is now payable only in Canadian currency—in 1931 less than one-third was in this position. Municipal debt which in 1930 was nearly 50 per cent more than that of Quebec was less in 1937, and was being reduced at a rate of approximately 3 per cent per annum. The reduction is particularly striking in the case of highway debt incurred in the middle twenties and repaid in a relatively short term by serial retirements.

Education and public welfare expenditures reflect the high level of real property taxation which has been established in Ontario, and also the greater than average financial assistance which the provincial government has given municipalities. Municipal expenditures on these services are some 28 per cent above the national average and provincial-municipal expenditures together 21 per cent higher. Nevertheless, Ontario has lost some of the outstanding lead enjoyed in these services in the twenties.

Relief expenditures in Ontario, particularly in the industrial centres which depended on the purchasing power of the rest of the country, reached \$60 million in 1934 but dropped relatively quickly to less than one-half that amount by 1937. In addition to the measure of general recovery experienced in that year, the unemployment situation in Ontario was greatly alleviated by the spectacular expansion of the mining industry, which both directly furnished employment in the mines and stimulated supply and construction industries and incomes generally throughout the Province.

The expanding frontier provided a useful outlet for both provincial and municipal public works. Experience has shown how costly is a policy of attempting to meet unemployment by provision of unnecessary public works. Generally speaking, provincial and municipal governments had made what were considered to be adequate capital provision for the times during the twenties. When the depression struck, these facilities were in many cases found to be more than adequate and drastic retrenchment became the rule. Municipalities on whom the burden of unemployment first fell were thus led to undertake unnecessary projects and manufacture "boondoggling" jobs. Even at the peak this policy provided for only a small proportion of the total number on relief¹⁹ and the cost and resulting deadweight debt burden proved out of all proportion to the cost of the alternative method of direct relief. This was partly because the municipality was a most inappropriate unit to plan and time suitable public works, and its credit base was too restricted to permit the necessary amount of deficit financing. The same considerations applied, although to a lesser extent, when provinces stepped in and adopted similar policies after municipalities had come to an end of their resources. In brief, in the absence of any long range and comprehensive planning of public works and administration by the Federal Government, which alone could pursue appropriate monetary policies to finance them, relief works programs by provincial and municipal gov-

ernments were desirable only where some real need existed for new public works. We have already noted that the need for modern highways in the Maritimes provided an opportunity for a large-scale and basically sound public works policy. The mining development in Northern Ontario likewise created a need for both provincial and municipal works (roads, schools, etc.) and for this reason Ontario was able to resort to a public works policy more advantageously than other provinces.

On agriculture and public domain Ontario has found it necessary to make relatively small net expenditures, although the contribution of the Hydro-Electric Power Commission of Ontario, the Temiskaming and Northern Ontario Railway, and the Ontario Farm Loans Board to the development of the Province's resources should not be overlooked. It has already been noted that Ontario may not, however, be making adequate provision for the conservation and most economic exploitation of its natural resources, or for the situation which will develop when some of these resources are exhausted. The transportation expenditures of Ontario governments reflect the stronger than average financial position of the municipalities and the earlier assumption by the provincial government of responsibility for planning and carrying out a comprehensive and suitable highway policy.

Summary

Any discussion of public finance in Ontario must be in the light of the superior position Ontario holds in the national economy. In the field of public finance this has been taken advantage of largely through heavy real property taxation. As a result Ontario municipalities as a whole, and services jointly shared by municipalities (education, public welfare and roads), are in a more comfortable financial position than in the rest of Canada. (There are, of course, important exceptions such as one-industry towns and some metropolitan suburbs.) This superior financial position, however, has been purchased at the expense of a frequently inequitable burden on one class of wealth. Because Ontario possesses such a large proportion of the taxable income of the Canadian economy, federal taxation policy is a factor of major importance in the Province's financial outlook. In the past a sufficient field has been left to provincial tax authorities to enable them, with relatively moderate taxation, to establish a level of governmental services above the average. However, intensive federal direct taxation, added to the already high level of property taxation, would severely pinch the provincial government.

¹⁹ Appendix 6—A. E. Grauer, *Public Assistance and Social Insurance*, p. 12.

MANITOBA

TABLE 97.—REVENUES ON CURRENT ACCOUNT—PER CAPITA, 1937

	Provincial and Municipal				Provincial		Municipal	
	\$ Per Capita		Percentage of Total Revenue		\$ Per Capita		\$ Per Capita	
	Man.	All Prov.	Man.	All Prov.	Man.	All Prov.	Man.	All Prov.
Real Property Taxes.....	23.71	22.60	48	45	1.03	0.53	22.68	22.07
Gasoline Taxes and Motor Vehicle Licences.....	5.08	5.84	10	12	5.08	5.84	—	—
Public Domain.....	0.84	1.90	2	4	0.84	1.90	—	—
Liquor Control.....	2.44	2.68	5	5	2.44	2.68	—	—
Miscellaneous Taxes, Licences, Fees, etc.....	6.73	6.85	14	15	1.48	1.64	5.25	5.20
Sub-Total.....	38.80	39.87	79	81	10.87	12.59	27.93	27.27
Sales Taxes.....	—	0.57	—	1	—	0.17	—	0.40
Corporation Taxes.....	2.58	3.06	5	6	2.58	3.06	—	—
Income Taxes on Persons.....	3.89	1.24	8	2	3.89	1.07	—	0.17
Succession Duties.....	0.56	3.22	1	6	0.56	3.22	—	—
Total Revenue from Provincial Sources.....	45.83	47.96	93	96	17.90	20.11	27.93	27.84
Federal Subsidies.....	3.42	1.91	7	4	3.42	1.91	—	—
TOTAL.....	49.25	49.87	100	100	21.32	22.02	27.93	27.84

Revenue System

An important factor in the provincial-municipal revenue system of Manitoba is the substantial yield of real property taxation, particularly in Winnipeg. Another factor of particular interest in comparison with other provinces is the emphasis on direct taxation. The provincial income tax, which was long the heaviest in North America on low salary brackets, and provincial succession duties raised nearly one-fifth of total provincial revenues in 1937. This seems a high figure for an agricultural economy, but it is due in some degree to a greater economic diversity than is perhaps generally appreciated, and

to the accumulation in the City of Winnipeg of a relatively large proportion of the surplus and taxable income of the Prairies. In addition, the provincial government took prompt and effective action to maintain revenues, and from their low point in 1931 provincial government revenues had recovered to the 1929 peak by 1933—the year in which aggregate provincial revenues touched their depression low and were some 20 per cent less than in 1929. In addition a special federal subsidy of nearly one-half again as much as the regular subsidy aided the provincial government in 1937. The revenue system of Manitoba has come through a period of abnormal strain as one of the soundest and most progressive in Canada.

TABLE 98.—EXPENDITURES ON CURRENT ACCOUNT—PER CAPITA, 1937

	Provincial and Municipal				Provincial		Municipal	
	\$ Per Capita		Percentage of Total Expenditure		\$ Per Capita		\$ Per Capita	
	Man.	All Prov.	Man.	All Prov.	Man.	All Prov.	Man.	All Prov.
Net Debt Charges.....	10.39	9.52	21	20	5.16	4.69	5.23	4.94
Public Welfare—								
Relief.....	6.25	5.45	14	11	4.10	3.86	2.86	1.59
Other.....	7.47	7.26	15	15	4.45	4.05	3.01	3.21
Education.....	9.63	9.78	20	20	2.33	2.89	7.30	6.89
Agriculture and Public Domain.....	1.02	1.86	2	4	1.02	1.86	—	—
Transportation.....	4.04	5.03	8	10	1.25	2.27	2.79	2.75
General Government and Miscellaneous.....	9.24	9.80	20	20	2.69	3.77	6.56	6.03
TOTAL.....	48.75	48.70	100	100	21.00	23.29	27.75	25.41
Per Capita Provincial Income, \$.....	361	345	—	—	—	—	—	—
Per Capita Outstanding Debt, \$.....	292	291	—	—	171	177	122	115
Percentage of Current Expenditure to Provincial Income.....	14	14	—	—	6	7	8	7
Percentage of Outstanding Debt to Provincial Income.....	81	84	—	—	47	51	34	33

Expenditures

Net debt charges (of provincial and municipal governments) roughly doubled in the early thirties, but in recent years have shown no increase. The provincial government's debt increase (1929-1937—\$21 million) was almost entirely due to relief costs, and all capital expenditures were drastically curtailed. Although Manitoba's credit weakness prevented the government from making any economies through debt refunding, the new borrowing was done from the Dominion on 3 per cent Treasury Bills. Virtually all the outstanding 6 per cent bonds mature by 1947, but the major proportion of the 4½, 5 and 5½ per cent bonds do not mature until the fifties, and two-thirds of the debt is optionally payable in currencies other than Canadian currency. The interest charges are consequently rigid and vulnerable to exchange movements. The outstanding municipal debt, in spite of the pressure of relief costs on Winnipeg and of the drought in the southwestern corner of the Province, was reduced nearly 10 per cent from 1930 to 1937, owing largely to repayment of debt incurred for highway and public utilities.

Provincial and municipal expenditures on education and welfare (excluding relief) were reduced approximately 10 per cent from 1930 to 1937

although aggregate expenditures of all provinces and municipalities rose 5 per cent during this period. At the present figure Manitoba's expenditures on these services are almost exactly the Canadian per capita average, although there are some factors which would tend under normal circumstances to make them above the average. For example, in Manitoba, as in the other western provinces, there is a lack of privately endowed universities, hospitals, and other communal facilities which imposes a heavier burden on public funds than in the eastern provinces.

The major relief problem has been in the metropolitan area of Winnipeg, although drought relief was necessary in the southwestern municipalities, and the chronic distress of the interlake region grew worse. Winnipeg (and its suburbs) inevitably suffered heavily from its great dependence on the Prairie wheat industry, and in addition became the natural rallying point for the large body of floating labour which is such an essential element in the Prairie economy. Crop failures and the cessation of virtually all construction activities left this group destitute and added to the already serious unemployment problem of the Winnipeg area. A larger than average share of relief costs was left to municipalities (1930-1937—27 per cent as compared with

the national average of 18 per cent) partly because Winnipeg's own financial position at the beginning of the depression was very strong. Several of its dormitory suburbs, however, entered the depression in a weak condition and, as their taxable capacity diminished almost as rapidly as relief costs grew, they were quickly forced into bankruptcy. The experience was both an indictment of the policy of leaving the costs of climatic and international trade disasters to small and arbitrarily segregated units, and of the obsolete form of municipal organization of metropolitan areas. The very good crops in recent years, combined with more than average severity of taxation and retrenchment of expenditure, permitted the provincial government and most of the municipalities to finance their shares of relief costs but at the expense of creating a sense of unjust and illogical treatment.

Expenditures on general government, public domain, and highway maintenance all reflect the severe policy of retrenchment pursued by the Manitoba Government. In some cases essential main-

tenance expenditures have been deferred to an extent which will prove costly in the long run. In the field of development there would appear to be room for some productive expansion of expenditure.

Summary

The financial position of Manitoba Governments reflects a picture of a very hard hit economy. The governments, however, rigorously reduced expenditures, discovered some unsuspected reserves of strength, and promptly chose a direct and efficient, although not particularly popular, method of maintaining revenues. These measures, with Dominion assistance, sufficed to weather the worst of the storm and Manitoba has recently been favoured with exceptionally good crops. Manitoba remains handicapped, however, by a rigid public debt structure and by a chronic metropolitan unemployment problem which affects the suburban municipalities in particular. Continuation of the present conditions threatens the credit and financial stability of both provincial and local governments.

SASKATCHEWAN

TABLE 99.—REVENUES ON CURRENT ACCOUNT—PER CAPITA, 1937

	Provincial and Municipal				Provincial		Municipal	
	\$ Per Capita		Percentage of Total Revenue		\$ Per Capita		\$ Per Capita	
	Sask.	All Prov.	Sask.	All Prov.	Sask.	All Prov.	Sask.	All Prov.
Real Property Taxes.....	17.55	22.60	43	45	1.03	0.53	16.52	22.07
Gasoline Taxes and Motor Vehicle Licences.....	3.81	5.84	10	12	3.81	5.84	—	—
Public Domain.....	0.85	1.90	2	4	0.85	1.90	—	—
Liquor Control.....	1.35	2.68	3	5	1.35	2.68	—	—
Miscellaneous Taxes, Licences, Fees, etc.....	7.75	6.85	19	15	1.87	1.64	5.88	5.20
Sub-Total.....	31.31	39.87	77	81	8.91	12.59	22.40	27.27
Sales Taxes.....	1.38	0.57	3	1	1.38	0.17	—	0.40
Corporation Taxes.....	1.30	3.06	3	6	1.30	3.06	—	—
Income Taxes on Persons.....	0.38	1.34	1	2	0.38	1.07	—	0.17
Succession Duties.....	0.26	3.22	1	6	0.26	3.22	—	—
Total Revenue from Provincial Sources.....	34.63	47.96	85	96	12.23	20.11	22.40	27.64
Federal Subsidies.....	5.98	1.91	15	4	5.98	1.91	—	—
TOTAL.....	40.61	49.87	100	100	18.21	22.02	22.40	27.64

Revenue System

The Saskatchewan débâcle is so well known that it is unnecessary to labour the point that statistical comparisons between Saskatchewan and other provinces for recent years are unrealistic. The per capita income of Saskatchewan, which for years exceeded the national average, was in 1937 only two-thirds of that average and, with the exception of Prince Edward Island, much the lowest in Canada. The revenue structure in Saskatchewan has been influenced by the nature of the economy and by the fact that during the period of expansion a few relatively simple tax measures yielded sufficient revenues to finance governments which were in general most economically administered. Our comparison shows that real property taxation in Saskatchewan was about three-quarters of the national per capita average in 1937, but this comparison is based on tax levies rather than on cash collections, and in 1937 only one-third of the municipal levy was collected. The other tax sources also tend to yield much less than the national average. Gasoline tax returns, for example, are reduced by exemptions for farm use; public domain revenues are low because of the limited range of resources and their unfavourable economic position at present; liquor profits are low because of the lack

of purchasing power under present conditions; progressive taxation (income taxes and succession duties), in spite of high rates, yields relatively negligible returns, and the same circumstances—the lack of any individual or corporate concentration of wealth in Saskatchewan—restrict corporation tax yields similarly. The sales tax is an effort to broaden the base of taxation. It is more appropriate in an economy such as that of Saskatchewan's than it would be in other provinces, and has been productive in circumstances in which few other taxes could have been, but it cannot be looked on as a desirable permanent feature or precedent.

The marvel is not that Saskatchewan's revenues fell, but that they did not fall more. Provincial revenues, in fact, rose slightly between 1930 and 1937, and municipal revenues, on an accrual basis, fell only one-quarter. In 1937, 15 per cent of total provincial-municipal revenues was provided by the federal subsidy (including the special temporary grant). The special subsidy, the Dominion loans to the Province (and the subsequent write-offs), and the Dominion assumption of relief responsibility in the drought area form the leading example of the arbitrary financial transfers necessary on occasion, under the present division of powers and responsibilities, to maintain the framework of government.

TABLE 100.—EXPENDITURES ON CURRENT ACCOUNT—PER CAPITA, 1937

	Provincial and Municipal				Provincial		Municipal	
	\$ Per Capita		Percentage of Total Expenditure		\$ Per Capita		\$ Per Capita	
	Sask.	All Prov.	Sask.	All Prov.	Sask.	All Prov.	Sask.	All Prov.
Net Debt Charges.....	9.37	9.52	19	20	6.48	4.59	2.90	4.94
Public Welfare—								
Relief.....	11.44	5.45	23	11	10.91	3.86	0.53	1.59
Other.....	7.18	7.26	14	15	3.85	4.05	3.34	3.21
Education.....	8.72	9.78	18	20	3.36	2.89	5.36	6.89
Agriculture and Public Domain.....	1.35	1.86	3	4	1.35	1.86	—	—
Transportation.....	3.04	5.03	6	10	1.39	2.27	1.65	2.75
General Government and Miscellaneous.....	8.41	9.80	17	20	3.24	3.77	5.15	6.03
TOTAL.....	49.51	48.70	100	100	30.58	23.29	18.93	25.41
Per Capita Provincial Income, \$.....	208	345	—	—	—	—	—	—
Per Capita Outstanding Debt, \$.....	291	291	—	—	230	177	62	115
Percentage of Current Expenditure to Provincial Income.....	24	14	—	—	15	7	9	7
Percentage of Outstanding Debt to Provincial Income.....	141	84	—	—	111	51	30	33

Expenditures

The provincial government's debt interest charges (gross and net) tripled between 1930 and 1937, but an actual reduction in municipal debt charges has restricted the increase of aggregate provincial-municipal debt service during this period to little more than \$3 million (\$5.6 million to \$8.8 million). Even at the present figure the joint provincial-municipal debt (which is almost exactly the national per capita average) is not alarming, except in relation to the abnormally low provincial income of recent years. Any reduction through normal refunding processes of the interest rate on Saskatchewan's outstanding funded debt was not, of course, possible in the circumstances of the thirties, but the great bulk of the new debt consisted of Treasury Bills sold to the Dominion at artificially favourable rates, and interest on these has been paid by further Treasury Bill issues. Borrowing from the Dominion for relief purposes up to 1937 was greater than the total provincial debt in 1929. Slightly more than one-half the provincial funded debt is in optional payment securities and two-thirds of the 4½ per cent and higher coupon bonds do not mature until the 1950's or later, thus introducing certain uncontrollable and rigid factors. But the special write-offs which the Dominion has already made on certain of its loans to Saskatchewan, the capitalization of interest due to the Dominion, and the assumption by the Dominion of the total costs of relief in the drought area all indicate that Saskatchewan's debt is considered as being in a special category, and can scarcely be appraised by conventional criteria. Although the financial position of Saskatchewan municipalities is desperate it is not revealed in their debt position because borrowings were held down to very moderate amounts during the twenties, and their credit was such that they simply could not borrow during the thirties.

Expenditures on education and public welfare (excluding relief) were cut between 1930 and 1937 by one-quarter. Education was particularly hard hit—joint provincial-municipal expenditures on education were reduced 40 per cent and rural municipal expenditures were cut by two-thirds. In the long run, when the personnel affected can find alternative employment, these reductions must produce serious deterioration in standards, and, as we have observed elsewhere, this concerns not only Saskatchewan but the whole country. The reduction in public welfare expenditures at a time when needs were increasing on a gigantic scale is the cold statistical reflection of a tremendous amount of

human misery. It is not a surprising, although a tragic, commentary that the pressure on mental institutions became particularly acute and beds are lacking for one-third of the serious cases. It is true that expenditures on a per capita basis are not materially below the Canadian average, but in relation to the needs (and in relation to the previous standards which were maintained) they are pitifully inadequate.

Relief expenditures in Saskatchewan reached fantastic levels. In 1937, when two-thirds of the population were on relief, relief expenditures by all governments in Saskatchewan were double total provincial and municipal revenues, excluding subsidies. A great proportion of the burden was for agricultural aid, and the necessity of supplying the operating costs for the major industry, rather than merely subsistence for individuals, involved huge amounts of money. There is ground for serious criticism of the methods adopted. Although the Dominion had to supply the bulk of the funds, the loans to farmers were made through provincial and municipal agencies, and the unpopular task of collecting the loans to reimburse the Dominion was also in their hands; there is some reason for believing that they engaged in the former function with far more enthusiasm than in the latter. Of much greater importance than the inevitable financial losses in such a system was the penalty imposed on individual honesty and self-reliance. From the point of view of Dominion-provincial relations and the smooth working of the federal system the creation of a huge amount of inter-governmental debt, and the financial dependence of Saskatchewan on the Dominion were threatening. In addition to the necessity for agricultural aid in the drought area, which it could be hoped was a temporary phenomenon, it became evident that in some areas of submarginal land a large proportion of the population would have to be moved. The provincial government of course has not had the funds, either to attempt to rehabilitate the depressed areas or to transfer people to undeveloped northern lands and equip and support them on the necessary scale.

Expenditures on general government, agriculture, public domain and highways all reflect drastic retrenchment. Highway maintenance expenditures were cut most severely—from 1930 to 1937 by 45 per cent. These cuts fell on a province which had never, except for a brief period in the early thirties, been a lavish spender, and they have consequently reduced expenditures in many cases below the desirable minimum level. The long-run costs of deferred maintenance threaten to be very great.

Summary

Saskatchewan presents the outstanding example of the unsuitability of the existing public finance system in emergencies,—but it must be admitted that almost any system would have broken down in the circumstances. However, when we consider the unfavourable economic prospects for Saskatchewan's major industry and the need for very large rehabilitation expenditures, it seems evident that Saskatchewan will not, under the present system, be able to assist the recovery of its economy or to

provide its population with services on a desirable scale. Although incomes are high in good years, they are not in easily taxable form, and there are no urban centres or corporate organizations of importance in Saskatchewan where surplus income accumulates and can be reached by provincial taxation. The rest of the country came to Saskatchewan's assistance on a very large scale in the emergency of the drought disaster, but there is serious danger that Saskatchewan will be left to its own inadequate resources to face the major long-run problems of readjustment and recovery.

ALBERTA

TABLE 101.—REVENUES ON CURRENT ACCOUNT—PER CAPITA, 1937

	Provincial and Municipal				Provincial		Municipal	
	\$ Per Capita		Percentage of Total Revenue		\$ Per Capita		\$ Per Capita	
	Alta.	All Prov.	Alta.	All Prov.	Alta.	All Prov.	Alta.	All Prov.
Real Property Taxes.....	22.35	22.60	45	45	1.52	0.53	20.83	22.07
Gasoline Taxes and Motor Vehicle Licences.....	5.63	5.84	11	12	5.63	5.84	—	—
Public Domain.....	2.17	1.90	4	4	2.17	1.90	—	—
Liquor Control.....	3.33	2.68	7	5	3.33	2.68	—	—
Miscellaneous Taxes, Licences, Fees, etc.....	8.03	6.85	16	15	3.28	1.64	4.75	5.20
Sub-Total.....	41.51	39.87	83	81	15.93	12.59	25.58	27.27
Sales Taxes.....	0.77	0.57	2	1	0.77	0.17	—	0.40
Corporation Taxes.....	2.74	3.06	5	6	2.74	3.06	—	—
Income Taxes on Persons.....	0.85	1.24	2	2	0.85	1.07	—	0.17
Succession Duties.....	1.70	3.22	3	6	1.70	3.22	—	—
Total Revenue from Provincial Sources.....	47.57	47.96	95	96	21.99	20.11	25.58	27.84
Federal Subsidies.....	2.28	1.91	5	4	2.28	1.91	—	—
TOTAL.....	49.85	49.87	100	100	24.27	22.02	25.58	27.84

Revenue System

The distinctive features of the Alberta revenue system include the survival of provincial real property taxation (as in Saskatchewan) and of some features of it which still show the influence of single tax theories. Progressive taxation, in spite of high rates (and in spite of an abnormally high succession duty payment in 1937), yields less than average. Corporation taxes have recently been sharply increased—a step influenced by more than simply revenue considerations. There was also a

short-lived experiment with a provincial retail sales tax in 1936 and 1937. The new Turner Valley oil field has been chiefly responsible for a rapid expansion in public domain revenues. Provincial revenues (excluding subsidies) dropped 23 per cent from 1929 to 1931, but since then have risen impressively and by 1937 were one-third above the 1929 peak, although provincial income was 30 per cent lower. Virtually all forms of provincial revenue show increases since 1929 with the exception of real property taxation. But, even the returns of this tax, both provincially and muni-

cipally, did not decline as much as might have been expected and total provincial-municipal revenues in 1937 were 7 per cent higher than in

1930. The fall in land values, however, has made the prevailing rates of property taxation extremely burdensome.

TABLE 102.—EXPENDITURES ON CURRENT ACCOUNT—PER CAPITA, 1937

	Provincial and Municipal				Provincial		Municipal	
	\$ Per Capita		Percentage of Total Expenditure		\$ Per Capita		\$ Per Capita	
	Alta.	All Prov.	Alta.	All Prov.	Alta.	All Prov.	Alta.	All Prov.
Net Debt Charges.....	7.55	9.52	17	20	4.58	4.59	2.97	4.94
Public Welfare—								
Relief.....	3.76	5.45	8	11	2.48	3.86	1.28	1.59
Other.....	7.11	7.26	16	15	3.82	4.05	3.28	3.21
Education.....	12.14	9.78	27	20	3.39	2.89	8.75	6.89
Agriculture and Public Domain.....	1.14	1.86	3	4	1.14	1.86	—	—
Transportation.....	5.35	5.03	12	10	1.72	2.27	3.63	2.75
General Government and Miscellaneous.....	7.66	9.80	17	20	3.00	3.77	4.67	6.03
TOTAL.....	44.71	48.70	100	100	20.13	23.29	24.58	25.41
Per Capita Provincial Income, \$.....	312	345	—	—	—	—	—	—
Per Capita Outstanding Debt, ^(a) \$.....	284	291	—	—	218	177	66	115
Percentage of Current Expenditure to Provincial Income ^(a)	14	14	—	—	6	7	8	7
Percentage of Outstanding Debt to Provincial Income ^(a)	91	84	—	—	70	51	21	33

^(a)Excludes unpaid interest.

Expenditures

National interest has been centred on Alberta's arbitrary reduction of debt charges. These have consistently been the highest of any province in Canada and it is perhaps not surprising that they were singled out for attack. Provincial net debt charges in 1930 were \$4.3 million annually, and in 1937 at full interest rates would have been (after adjustment for interest received) \$5.4 million; actually they were \$3.6 million. Only 22 per cent of the provincial funded debt is payable in Canadian currency only, and more than one-half the debt bearing 4½ per cent coupon rates or higher does not mature until after 1950. It is consequently evident that the provincial debt at its original coupon rates was in a technically rigid and vulnerable position, and only small reductions in carrying charges would have been possible through orderly refunding. Municipal debt is substantially below the Canadian average and per capita municipal debt charges in 1937 were only one-half the average. This is in part due to reorganization of the Calgary and Edmonton debts. The outstanding debt of

rural municipalities is negligible. Roughly speaking, the savings from the interest cut have been used to pay for relief, thus holding debt increases on this account below the average. In addition, capital expenditures have been held down to moderate levels, resulting in the lowest over-all debt increase for combined provincial and municipal governments during the depression in any province except Manitoba.

Expenditures on welfare (excluding relief) and education are still 13 per cent above the national per capita average, although they have declined 3 per cent as compared with a nation-wide increase of 5 per cent between 1930 and 1937. Expenditures by the provincial government on these services have been increased, offsetting part of the enforced reduction in municipal expenditures on education. Certain factors, such as the cost of living and the scattered nature of settlement, tend to make the costs of these services higher than average in order to provide equal standards. In addition, Alberta has experimented more freely than most other provinces with advanced forms of public welfare

and educational services. In this, as in the provision of community equipment, Alberta has consistently shown an inclination, characteristic of newly opened and rapidly developing economies, to use community effort and credit to accelerate development and provide the amenities of life. This policy inevitably involves, of course, a higher level of governmental overhead, but may in return provide a higher real provincial income.

Agricultural relief has been a serious problem in Alberta, although owing to materially better crops and greater diversification than in Saskatchewan not on the same tremendous scale as in that Province. Distress was caused by the combination of ruinously low prices and what are probably the highest fixed charges (in the form of agricultural indebtedness, railway freight rates, irrigation investments and government indebtedness) in Canada rather than by climatic disaster. The provincial government, which supplied the bulk of the funds necessary for agricultural relief, collected a much higher proportion of its advances than did Saskatchewan, where Dominion funds were re-loaned, in part because of the better crops in Alberta and the reduction in private debt charges. In Edmonton and Calgary, Alberta has a problem somewhat similar to that of Winnipeg's, although on a much smaller scale, as the unemployed floating labour of the Western Provinces tend to congregate there. The Turner Valley oil development and the mining activity in the Northwest Territories alleviated the problem in Calgary and Edmonton, but only to a limited extent. Advances to these cities of more than \$2½ million were made by the provincial government but nevertheless the burden proved excessive, and they were forced to reduce their debt charges. The Government's arbitrary reduction of interest rates has had important and probably unexpected reactions on the method of financing relief. In 1937 (i.e. fiscal year 1937-38), which was the first period in which the full effect of the halving of interest rates on government bonds was reflected in the budget and the latest period for which complete statistics on relief expenditures are available, the Province and municipalities spent some \$4 million on relief from their own funds. The provincial government reduced interest payments by \$3.4 million. In brief, relief was financed by a

forced levy on bondholders rather than, as in other Western Provinces, by advances from the Dominion; from an immediate cash point of view the beneficiary of the Alberta action was the Dominion government which was relieved of the necessity of making further loans to the province, although it was the provincial government which bore the stigma of default.

Expenditures on public domain, agriculture and highways are influenced by the fact that Alberta possesses the last important undeveloped agricultural frontier in Canada. Development of this frontier, and also of the newly discovered mineral and oil resources, calls for substantial capital investment and for increased expenditures on current account. The nature of the terrain and the long distances which separate the settled areas make the provision and maintenance of highways more costly than average.

Summary

Alberta's financial position should be considered in relation to its present economy and its potential development, as well as to the condition of default which now exists. High debt charges have unquestionably been an outstanding and important characteristic, not only of Alberta public finance but of the whole economy, and they become extremely serious when income falls sharply. The pressure is intensified, of course, by the fact that most of the debt is held externally and the creditors are consequently not subject to the jurisdiction of Alberta taxing authorities. In these circumstances the rigidity of the debt structure will, on occasion, put great pressure on the economy, and, as a natural reaction, make the position of creditors highly vulnerable. A more elastic and appropriate form of financing than that of fixed interest rates for agriculture and other economic activities would add greatly to the Province's prospects of financial stability. The need for additional capital to finance the development which Alberta's resources would apparently justify makes this an extremely important factor. With a private and public financial structure designed in relation to its regional characteristics and economic disabilities, Alberta should be able to maintain a high standard of living and of community services.

BRITISH COLUMBIA

TABLE 103.—REVENUES ON CURRENT ACCOUNT—PER CAPITA, 1937

	Provincial and Municipal				Provincial		Municipal	
	\$ Per Capita		Percentage of Total Revenue		\$ Per Capita		\$ Per Capita	
	B.C.	All Prov.	B.C.	All Prov.	B.C.	All Prov.	B.C.	All Prov.
Real Property Taxes.....	26.11	22.60	38	45	2.74	0.53	23.37	22.07
Gasoline Taxes and Motor Vehicle Licences.....	8.03	5.84	12	12	8.03	5.84	—	—
Public Domain.....	5.88	1.90	8	4	5.88	1.90	—	—
Liquor Control.....	5.45	2.68	8	5	5.45	2.68	—	—
Miscellaneous Taxes, Licences, Fees, etc.....	7.70	6.85	11	15	3.62	1.64	4.08	5.20
Sub-Total.....	53.17	39.87	77	81	25.72	12.59	27.45	27.27
Sales Taxes.....	—	0.57	—	1	—	0.17	—	0.40
Corporation Taxes.....	9.25	3.06	13	6	9.25	3.06	—	—
Income Taxes on Persons.....	2.67	1.24	4	2	2.67	1.07	—	0.17
Succession Duties.....	1.90	3.22	3	6	1.90	3.22	—	—
Total Revenue from Provincial Sources.....	66.99	47.96	97	96	39.54	20.11	27.45	27.84
Federal Subsidies.....	2.16	1.91	3	4	2.16	1.91	—	—
TOTAL.....	69.15	49.87	100	100	41.70	22.02	27.45	27.84

Revenue System

The most striking feature in the above table is the comparison between the per capita revenues of the provincial government of British Columbia and the average for all Canadian provinces. The British Columbia figure is nearly double the average. Municipal revenues are at the Canadian average, although a smaller portion of British Columbia is municipally organized than is the case in most provinces.

Nearly all the revenue sources produce higher returns than in the rest of Canada, but the most striking lead is in corporation taxation and public domain revenues. These are three times the Canadian average in yield per capita. They are made possible by the richness of some of British Columbia's natural resources and the highly concentrated corporate form of organization which has been adopted to exploit them. Gasoline taxes, liquor control profits and real property taxation all substantially exceed national averages and reflect the higher per capita income and purchasing power in British Columbia. On the other hand, succession duty yields are little more than half the national

average, in part because sufficient time has not yet elapsed for the accumulation of large individual fortunes, and in part because provincial policy has been to encourage migration to the coast of wealthy retired people. Revenues, and particularly provincial corporation, gasoline, liquor control and public domain revenues, showed remarkable recovery from the low point in 1933. Provincial revenues in 1937 were almost one-quarter more than in 1929. Owing to a fall in real property tax yields in Vancouver, however, there was a slight decline in total municipal revenues, and aggregate provincial-municipal revenues increased only some 11 per cent between 1930 and 1937, or slightly less than the increase for all provinces and municipalities. The dominating importance of corporation taxes and public domain revenues will be noted from the foregoing table. These two revenue sources, on a per capita basis, are three-fourths as much as the total provincial government revenues of all provinces, or nearly as much, for example, as the total provincial government revenues of Quebec. They reflect the higher than average return derived from the large-scale development of British Columbia's natural resources

made possible in the last two decades by technological advances and important reductions in ocean freight rates. Many of these resources are of a wasting character, and it has evidently been the Province's policy to secure a substantial share of the profits derived from their exploitation while it has the opportunity. In addition to the direct return derived by the provincial government from its natural resources, the higher than average income in British Columbia is based to an important extent on their very rapid development and on the ancillary construction industry activity in the last two

decades, and this income is reflected in the generally high yield of consumption and other taxes.

The provincial income tax, which was the first to be imposed in Canada, starts at a relatively low figure (single person's exemption \$600) and progresses to a rate of 10 per cent on all taxable income plus a surtax rising to 18 per cent on large incomes. As no exemption is allowed for Dominion income tax payments,* the tax is a relatively heavy one on higher incomes. It has proved a stable source of revenue, and yields substantially more per capita than does the Ontario income tax, for example, but the double taxation involved is resented.

TABLE 104.—EXPENDITURES ON CURRENT ACCOUNT—PER CAPITA, 1937

	Provincial and Municipal				Provincial		Municipal	
	\$ Per Capita		Percentage of Total Expenditure		\$ Per Capita		\$ Per Capita	
	B.C.	All Prov.	B.C.	All Prov.	B.C.	All Prov.	B.C.	All Prov.
Net Debt Charges.....	14.37	9.82	21	20	8.71	4.59	5.66	4.94
Public Welfare—								
Relief.....	6.09	5.45	9	11	5.09	3.88	1.00	1.59
Other.....	10.47	7.26	15	15	6.25	4.05	4.22	3.21
Education.....	12.47	9.78	18	20	5.69	2.89	6.78	6.89
Agriculture and Public Domain.....	2.53	1.86	4	4	2.53	1.86	—	—
Transportation.....	6.18	5.03	9	10	3.83	2.27	2.35	2.75
General Government and Miscellaneous.....	15.74	9.80	24	20	7.04	3.77	8.70	6.03
TOTAL.....	67.85	43.70	100	100	39.14	23.29	28.71	25.41
Per Capita Provincial Income, \$.....	425	345	—	—	—	—	—	—
Per Capita Outstanding Debt, \$.....	379	291	—	—	238	177	141	115
Percentage of Current Expenditure to Provincial Income.....	16	14	—	—	9	7	7	7
Percentage of Outstanding Debt to Provincial Income.....	89	84	—	—	56	51	33	33

Expenditures

Per capita net debt charges of combined provincial and municipal governments are 50 per cent above the Canadian average, but they increased only 10 per cent between 1930 and 1937 as compared with an average increase of 24 per cent. These charges have, in fact, declined slightly since 1932, when the premium on foreign exchange was an important item. Virtually all net increase in debt since 1933 has been borrowed from the Dominion on 3 per cent Treasury Bills, but some public borrowing, largely for refunding purposes, has also been done at 3 and 3½ per cent. There has also

been some reduction in recent years in the outstanding provincial debt payable abroad but nearly four-fifths of the funded debt is still optionally payable in other than Canadian currency. Three-fifths of the provincial debt bearing 4½ per cent or higher coupons matures before 1950, with particularly large maturities in the early forties. The Government has maintained large cash balances and sinking funds in preparation for these maturities, and its technical position to refund them on

* Although income taxes paid by B.C. corporations to the provincial government are deductible from personal income taxes paid by B.C. dividend recipients.

advantageous terms would appear to be strong. There have been no significant variations in municipal debt in recent years.

Expenditures on education and public welfare (excluding relief) are about one-third above the national per capita average, although they do not absorb quite as large a proportion of total municipal-provincial revenues as in other provinces. The notably high return from public domain and corporation taxation has made it possible for the Province to provide higher than average services, and has enabled the provincial government to contribute a substantially larger proportion of the total than in any other province (except Prince Edward Island). This is particularly notable in the case of education, where the provincial government provides 45 per cent of the expenditure as compared with an average contribution of 30 per cent. In several important fields of public welfare British Columbia has pioneered and this, coupled with higher costs of living and of salaries and the sparseness of the population outside the metropolitan area of Vancouver, has contributed to the higher than average costs in British Columbia. However, even after allowing for these factors, it would seem clear that British Columbia provides better than average standards in these services.

Relief costs in British Columbia rose sharply at the beginning of the depression, and have throughout been substantially more than the national average. Although they were not as severe in relation to provincial income as in the Prairie Provinces, the Province was forced to resort to borrowing from the Dominion as early as 1931 and, in spite of the buoyant revenues of recent years, the relief burden has prevented the complete re-establishment of provincial credit. The extreme depression in the primary exporting industries (and in those supplying the Prairies), the impact on the service, supply and shipping industries of Vancouver, the immigration of unemployed attracted by the coast climate, and the higher standards maintained, all intensified the problem. In common with the rest of the country public works were undertaken on a large scale in the early years of the depression, but since 1932 the bulk of the expenditure has been on direct relief. However, since 1935 the municipal proportion of the total burden has declined as rapidly rising provincial revenues enabled the provincial government to assume a larger share. In addition, provincial government expenditures on public works, which were reduced to virtually nothing in the depths of the depression, have

recovered to approximately pre-depression levels and have been a factor in reducing unemployment.

Expenditures on public domain and transportation, as might be expected from the topographical nature of the Province and the importance of developing its great but sometimes almost inaccessible resources, exceed the average per capita expenditures. It would seem clear that substantial additional expenditures on conservation of some types of resources, and on development of alternative means of livelihood for the population dependent on the exhaustible resources, will be necessary.

Expenditures on general government are strikingly higher than average. They are more than double the expenditures in the three Maritime Provinces together, for example, and nearly double expenditures in Manitoba or Alberta, which have each approximately the same population. To some extent this may be explained by the higher costs arising from the nature of the country, and from higher salaries necessary in order to develop a competent Civil Service in step with the rapid expansion of the Province, but the 10 per cent increase in these expenditures between 1930 and 1937 compares with a 4 per cent decrease in expenditures on general government by all Canadian governments over the same period.

Summary

British Columbia's high provincial income combined with its high rates of taxation yields a very much larger than average government revenue, and have made possible the provision of government services of superior standard. To an important extent, however, the Province has been living on its capital, and it can scarcely be expected that the fortuitous coincidence of economic events of the last two decades which proved so stimulating and advantageous to British Columbia will be repeated. The necessity for amortizing debt incurred for developmental projects, and particularly for those such as the Pacific Great Eastern which have already proved ill-advised and unproductive, before the best of the resources are exhausted, is clear. Equally important is the most economic utilization of the remaining resources, and the development of ways and means of strengthening the economy for the future. The high and apparently rigid character of governmental overhead costs will be a serious liability when resources are depleted, particularly as the present revenue system, which has been so strikingly productive in recent years, would in these circumstances be seriously crippled. However, in the

meantime British Columbia residents have the advantage of better education and better communal services than has the average Canadian citizen, and they have shown a willingness to maintain these standards by submitting to higher than average taxation.

5. THE CONTRAST: CONFEDERATION AND TODAY

Within the brief compass of the preceding chapters we have attempted to portray the significant economic, financial, political and social changes which constitute the background of the present problems of Dominion-provincial relations and public finance. To obtain a proper understanding of those problems we have found it necessary to survey the history of Confederation, and to analyse the factors which have determined the course of Canadian development and have made Canada what it is to-day. We have outlined the forces which brought about Confederation, the federal distribution of financial powers and responsibilities which was set up in 1867, and the political and economic objectives of the new self-governing

British Dominion in North America. We have described, with particular reference to the working of the federal fiscal system, how, within that political framework, the isolated regions and pockets of settlement with a population of less than three and a half millions have grown into an integrated transcontinental economy with a population of eleven millions; how small towns and cities have grown into large urban concentrations and great metropolitan centres; how the self-sufficiency of the household and the family has been superseded by highly specialized activities which are closely dependent upon the smooth operation of an intricate exchange economy; how the meagre but relatively stable incomes have risen to support a much higher but more precarious standard of living; and finally how the philosophy of government has changed from one of laissez-faire to one of increasing interference with a view to improving economic and social conditions. These far-reaching changes have had a profound effect upon public finance, and particularly upon that of our federal system.

TABLE 105.—THE GROWTH OF GOVERNMENT EXPENDITURES SINCE CONFEDERATION AND THE INCREASING SHARE BORNE BY THE PROVINCES AND MUNICIPALITIES

(Millions of Dollars)

	Total ^(a)		Dominion		Provinces		Municipalities		Percentage of Dominion to the Total	
	1874	1937	1874	1937	1874	1937	1874	1937	1874	1937
Net Debt Charges.....	6.6	271.3	5.4	167.0	0.6	50.9	1.8	54.8	82	62
National Defence and War Pensions.....	1.3	88.0	1.3	88.0	—	—	—	—	100	100
Public Welfare—										
Relief.....	—	126.6	—	66.1	—	42.9	—	17.6	—	52
Other.....	1.4	124.4	0.2	43.8	0.7	45.0	0.5	35.6	14	35
Education.....	3.0	108.9	—	—	1.4	32.1	1.6	76.5	—	—
Highways and Transportation.....	5.4	73.8	2.8	18.0	1.2	25.2	1.4	30.6	52	24
Highways and Transportation (including debt charges).....	(9.8)	(240.4)	(7.2)	(143.0)	(1.2)	(51.6)	(1.4)	(45.8)	(73)	(59)
Public Domain and Agriculture.....	1.6	38.5	0.9	17.9	0.7	20.6	—	—	56	46
General Government and Miscellaneous.....	12.6	164.6	6.0	56.2	3.9	41.8	2.7	66.9	48	34
Subsidies to Provinces.....	—	—	3.8	21.2	—	—	—	—	—	—
TOTAL.....	31.9	996.1	20.4	478.2	7.3	258.5	8.0	282.0	64	48
Total Expenditures Per Capita, \$.....	8.19	89.58	5.24	43.00	1.87	23.25	2.05	25.36	—	—
Percentage of Total Expenditures to the National Income.....	9%	26%	6%	12%	2%	7%	2%	7%	—	—

^(a) Less Duplications.

^(b) Estimated.

The revolutionary change since Confederation in the economic and social role of government is strikingly illustrated in Table 105 above. Between 1874 and 1937 total per capita government expenditures increased by eleven times. The portion of the national income spent by governments rose from less than one-tenth to more than one-fourth of the total. The collective efforts to promote economic development and the collective assumption of the responsibility for the alleviation of individual distress and for the provision of rising standards of public welfare and education have come to play an immensely important part in the economic affairs of the country—a part which could hardly have been envisaged at the time of Confederation and provided for in the framing of the constitution. The amounts expended to promote economic development, added to debt charges arising out of war and deficits, have risen from \$14 million to \$384 million. The cost of education and public welfare rose from the almost negligible figure of \$4 million to \$360 million. Such increases would in any case have created difficult problems for public finance, but under the federal system these difficulties were greatly enhanced. The division of powers and responsibilities devised at Confederation was made on the basis of conditions existing at the time. The Federal Government was charged with the responsibilities which were then national in scope—of which defence and economic development were the most important—and the provinces and their municipalities with responsibilities which were then predominantly local in nature, including education, public welfare and local works. The growth in government expenditures and functions has not fitted the simple pattern which was set up in 1867. Government responsibilities which were formerly of purely local significance have become national in character. The provinces have assumed heavy commitments for economic development. The invention of the motor vehicle has added heavy burdens to provincial expenditures on transportation. A number of essential or important public welfare services which have remained as primary obligations of local governments can now be provided efficiently only on a national basis. The provinces, which at the time of Confederation were not expected to incur any sizeable debts, had by 1937 assumed debt charges which absorbed over one-fifth of their current revenues. Public welfare, the outlay upon which was negligible in 1874, took more than one-third of the provincial revenues in 1937. Thus, expenditures which were virtually non-existent at Confederation absorbed nearly 60 per

cent of total provincial receipts on current account in 1937. The development of these expenditures by the provinces in addition to the share supported by their municipalities has greatly altered the relative importance of the different layers of government in our federal system. The share of the total costs of government borne by the Dominion, which possessed the broadest base of taxation, fell from two-thirds to less than one-half. Furthermore, an important part of the Dominion's outlay at the present time, namely for relief and old age pensions, is actually expended by the provinces.

The increase in revenues required to support the immense rise in government expenditures has placed a heavy strain on the constitutional division of powers adopted at Confederation. The revenue sources used in 1874 (of which customs and excise collected by the Dominion made up two-thirds of the total), provided only one-half of all government receipts in 1937 including the taxes on real estate which have continued to support virtually the whole of the great increase in municipal services. The Dominion, which in 1874 depended almost entirely on the essentially national revenue sources of customs duties and excises on a few luxuries, has expanded its income mainly by a heavy impost on general consumption, by levies on corporations and by the taxation of personal net incomes. The provinces, which at Confederation were given power to levy direct taxation, but were expected to rely on the fixed federal subsidies, and on receipts from public domain and from various licences and fees, obtained less than one-fourth of their income from these sources in 1937. The unconditional federal subsidies comprised nearly two-thirds of total provincial revenues in 1874 and less than one-tenth in 1937. The great bulk of the present provincial revenues is collected from sources which have been interpreted as falling under provincial jurisdiction but which could hardly, if at all, have been envisaged at Confederation. Some of these sources are directly competitive with those employed by the Dominion; many of the others constitute onerous or uneconomic levies on consumption and the costs of production. With the joint occupation of the field of direct taxes, neither the Dominion nor the provinces nor both together have been able to employ the progressive taxes to the extent which is economically and socially desirable.

It is clear that the present situation in Canadian public finance represents a wide departure from the conception of the Fathers of Confederation and from the spirit of the financial settlement which

TABLE 106.—GROWTH OF GOVERNMENT REVENUES SINCE CONFEDERATION
(Millions of Dollars)

	Total ^(a)		Dominion		Provinces		Municipalities		All Government Percentage to Total Revenues	
	1874	1937	1874	1937	1874	1937	1874	1937	1874	1937
<i>Revenue from Sources used at Confederation—</i>							^(b)			
Customs.....	14.4	112.1	14.4	112.1	—	—	—	—	46	11
Excise.....	5.6	52.0	5.6	52.0	—	—	—	—	18	5
Public Domain.....	1.8	23.6	0.4	2.5	1.4	21.1	—	—	6	2
Licences, Permits and Fees.....	1.2	21.9	—	2.5	0.7	8.9	0.5	10.5	4	2
Taxes on Real Property.....	6.5	250.8	—	—	—	5.9	6.5	244.9	21	25
Miscellaneous.....	1.5	39.1	0.4	10.2	0.1	3.3	1.0	27.0	5	5
Sub-Total.....	31.0	499.5	20.8	179.3	2.2	39.2	8.0	282.4	100	50
<i>Revenue from Sources Developed since Confederation—</i>										
Sales Taxes.....	—	144.4	—	138.1	—	1.9	—	4.4	—	15
Gasoline Taxes and Automobile Licences.....	—	64.8	—	—	—	64.8	—	—	—	6
Liquor Control.....	—	29.8	—	—	—	29.8	—	—	—	3
Manufacturers Taxes.....	—	17.2	—	17.2	—	—	—	—	—	2
Amusement Taxes.....	—	2.8	—	—	—	2.8	—	—	—	—
Miscellaneous Taxes.....	—	30.8	—	7.4	—	3.1	—	20.4	—	3
Corporation Taxes.....	—	105.7	—	71.7	—	34.0	—	—	—	11
Income Taxes on Persons.....	—	64.4	—	50.6	—	11.9	—	1.9	—	6
Succession Duties.....	—	35.8	—	—	—	35.8	—	—	—	4
Sub-Total.....	—	495.7	—	285.0	—	184.1	—	26.7	—	50
Total Revenues Raised by Each Class of Government.....	31.0	995.2	20.8	464.3	2.2	223.3	8.0	309.1	100	100
Federal Subsidies to the Provinces.....	—	—	—	—	3.8	21.2	—	—	—	—
GRAND TOTAL.....	31.0	995.2	20.8	464.3	6.0	244.5	8.0	309.1	100	100
Percentage of Revenue Raised by each Class of Government to Total.....	100%	100%	67%	47%	7%	22%	26%	31%	—	—

^(a) Less Duplications.
^(b) Estimated.

they devised. Costly government responsibilities which have become national in scope are being supported by regional and local revenues. Revenue sources which have become national in character are being employed by regional and local governments to the complete or partial exclusion of the central authority. We have seen that the efficient administration of the functions of government under present day conditions requires some redis-

tribution of the functions as between the Dominion and the provinces. In the same way, if the growing waste and inequities in taxation are to be avoided, a better allocation of taxing powers and responsibilities is imperative. A third essential step will be to adjust the revenue sources to the functions so as to ensure that every unit of government will be financially able to meet its recognized responsibilities.

CHAPTER IX

THE CONSTITUTION TO-DAY

In an earlier chapter the significant decisions on the meaning of the British North America Act given by the Privy Council before 1896 were briefly considered and their bearing on the future interpretation of the constitution was pointed out.¹ Between 1896 and the present the Privy Council has decided well over one hundred cases which involved the interpretation of various provisions of the British North America Act. Some of these cases dealt with matters of very minor importance but the vast majority of them have been woven into the texture of the constitution. An accurate and complete statement of what the constitution is at the present day must analyze these cases, considering the scope of the decisions and the qualifications, express or implied, imposed by later decisions on earlier ones. Such a minute examination is beyond the scope of this Report and would involve a lengthy excursion into constitutional niceties, of interest mainly to specialists.

But the interpretations of the Privy Council have marked out the limits of the legislative power of the Dominion and the provinces. Among other things, they have determined the scope of provincial taxing powers. In these ways the decisions of the Privy Council have fixed both the responsibility for carrying out new functions which it is considered desirable for governments to undertake and the limits of the revenue sources available to the province for financing its activities. In working within this framework to meet mounting demands for governmental action, many new aspects of Dominion-provincial relations have emerged. The interpretation of the constitution in relation to twentieth century demands has helped to shape the present financial relationships between the Dominion and the provinces and has led to the adoption of several expedients involving co-operative action by the Dominion and the provinces. These co-operative ventures have, in turn, complicated the relationships which the Commission is required, by its terms of reference, to examine.

Accordingly, a survey of the constitutional development is necessary for the understanding of present problems. It is also important to see how the provinces and the Dominion were forced into

these co-operative ventures and to appreciate the inherent difficulties which they involve. A short survey of constitutional developments cannot hope to deal adequately with many constitutional complexities. An attempt to state briefly how the constitution allots responsibility for dealing with the problems which absorb the attention of legislatures today must speak in general terms without exhaustive reference to the legal decisions in which these matters have been explained. It cannot state all the qualifications to which any general proposition is subject nor grapple with the obscurities which still undoubtedly exist. What follows is a summary of those aspects of the constitution relevant to the inquiry conducted by the Commission and not a full exposition of constitutional law.

The Restrictive Interpretation of Section 91

In its interpretation of the British North America Act in the last forty years, the Privy Council has adhered to the general rule of construction laid down by Lord Watson in the *Local Prohibition Case*² in 1896 which accorded Dominion legislation under the enumerated heads of section 91 primacy over the provincial powers set out in section 92 but denied this primacy to the general clause of section 91 which gave the Dominion power to make laws for the "peace, order and good government of Canada". This rule of construction, coupled with a broad interpretation of the general expression "property and civil rights in the province", contained in section 92, has given a narrow application to the so-called residuary clause in section 91. Accordingly, with rare exceptions, if a proposed piece of Dominion legislation does not fall within the specific enumerations of section 91, it is beyond the enacting power of the Dominion and within the powers of the separate provinces. That is to say, most of the novel legislation of our day, which is not of a type actually contemplated and expressly provided for by the framers of the British North America Act, must be enacted, if at all, by the provinces. There is much truth, as well as some exaggeration, in the contention that the "property and civil rights" clause has become the real residuary clause of the constitution.

¹ See pp. 30 f.

² See p. 58 for a discussion of this case.

The Dominion power under section 91 (2) "regulation of trade and commerce" has received a restricted interpretation, improving on the limitations suggested in *Citizens' Insurance Company v. Parsons*³ in 1882 until, in 1925, the Privy Council questioned whether it was operative at all as an independent source of legislative power.⁴ More recent decisions show that it has some scope⁵ but the narrow meaning given to it limits severely the power which it confers on the Dominion to regulate economic life.

The trend of interpretation, therefore, has been favourable to provincial power. However, between 1930 and 1932, the Privy Council handed down several decisions upholding Dominion legislation in a manner which seemed to involve qualifications on some of their earlier pronouncements⁶ and, at the same time, to countenance freer and looser interpretation of the British North America Act than had hitherto been adopted.⁷ Some regarded these decisions as marking a reversal of the trend of decision and a new emphasis on the scope and magnitude of Dominion powers. But this reversal of trend by the Privy Council, if reversal it was, turned out to be merely temporary, as its adverse decision in 1937 on a number of Dominion measures, commonly known as the Bennett "New Deal", clearly showed.

These decisions of 1937 scarcely came as a surprise but they served to underline again the wide scope of provincial powers and responsibilities in modern economic and social legislation. When related to the limitations on the taxing powers of the provinces under the British North America Act and the wide disparities in the yield of revenue sources in the different provinces, they placed the crisis which had been gathering in Canadian public finance in clear relief. In a sense, it may be said that these decisions framed the Commission's terms of reference and it is both appropriate and revealing that this discussion of the constitutional position today should revolve around them. With some reference to earlier decisions on particular points, a discussion of these cases illustrates the division of legislative power between the provinces and the Dominion in relation to the urgent issues of the present day.

³ See pp. 32-34 for these suggested limitations.

⁴ *Toronto Electric Commissioners v. Snider*, [1925] A.C. 396 at p. 410.

⁵ *Proprietary Articles Trade Association v. Attorney-General of Canada*, [1931] A.C. 310 at p. 326; *Attorney-General of Ontario v. Attorney-General of Canada*, [1937] A.C. 405.

⁶ *Proprietary Articles Trade Association v. Attorney-General of Canada*, [1931] A.C. 310; *In re Regulation of Aeronautics*, [1932] A.C. 64; *In re Regulation of Radio Communication*, [1932] A.C. 304.

⁷ See *Edwards v. Attorney-General of Canada*, [1930] A.C. 124.

In 1936 the constitutional validity of eight Dominion enactments was referred to the Privy Council and their decisions on them were rendered early in 1937.⁸ The validity of two of these statutes was upheld in full,⁹ and of one of them, in part.¹⁰ These three statutes are not highly important for our purposes and they need not be discussed in detail. But the nature and the fate of the remaining five require careful consideration.

Three of the remaining five enactments, the *Weekly Day of Rest in Industrial Undertakings Act*, the *Minimum Wages Act* and the *Limitation of Hours of Work Act*, established, as their titles indicate, nation-wide standards for minimum wages and maximum hours of weekly work. They were enacted by Parliament pursuant to obligations assumed by the Dominion under conventions of the International Labour Organization and were thus, in substance, in fulfilment of treaty obligations of Canada. All three were held by the Privy Council to affect "Property and Civil Rights in the Province" and, therefore, to be beyond the powers of the Dominion Parliament to enact.¹¹

Apart from the fact that the decision on these statutes denied the power of the Dominion to set up nation-wide standards of labour legislation, it established two general propositions of great significance. First, it interpreted section 132 of the British North America Act which empowers the Dominion Parliament to implement "the Obligations of Canada or of any Province thereof, as Part of the British Empire, toward Foreign Countries arising under Treaties between the Empire and such Foreign Countries." It held that the power of the Dominion under section 132 applies only to "British Empire treaties" negotiated by the Imperial Executive where the treaty obligations involved are assumed by Canada as part of the British Empire. In international treaties which the Dominion negotiates in its own right as an independent political unit, the power of the Dominion to implement the treaty by legislation depends entirely on whether the subject matter of the treaty falls within section 91 or section 92. That is to say, in view of the broad interpretation given to section 92, there are a number of matters on which

⁸ For a full discussion of these decisions, see the symposium by a number of leading constitutional authorities in [1937] 16 *Canadian Bar Review*, 401-507.

⁹ Reference *re Section 188A of the Criminal Code*, [1937] A.C. 268; Reference *re Farmers' Creditors Arrangement Act*, [1937] A.C. 391.

¹⁰ Reference *re Dominion Trade & Industry Commission*, [1937] A.C. 405.

¹¹ These three enactments were dealt with in a single opinion. See *Attorney-General of Canada v. Attorney-General of Ontario*, [1937] A.C. 326.

the Dominion cannot give effect to treaties which it alone has power to negotiate. The second proposition established by this decision is also involved in the decision on another of these statutes, the *Employment and Social Insurance Act*, and can be most conveniently discussed along with it.

The *Employment and Social Insurance Act* provided for a nation-wide system of unemployment insurance in specified industries to be supported, in part, by compulsory contributions of employers and employees and, in part, by contributions from the Federal Government. Such a scheme, the Privy Council held, was beyond the powers of the Federal Parliament to enact because it affected "Property and Civil Rights in the Province".¹² The argument that unemployment was a national evil, justifying national action under the "peace, order and good government" clause of section 91 was met by reference to a line of decisions holding that this clause of section 91 conferred on the Dominion an emergency power only.

In the interval between 1896 and 1937, Lord Watson's remark in the *Local Prohibition Case* that "some matters in their origin local and provincial might attain such dimensions as to affect the body politic of the Dominion and to justify the Canadian Parliament in passing laws for their regulation . . ." under the general clause of section 91 had been explained in several cases. In substance, these cases had decided that, during the stress of a severe crisis like the War of 1914-18, the Dominion Parliament had power to fix the prices of commodities and to regulate comprehensively other aspects of Canadian economic life under the "peace, order and good government" clause¹³ but that as soon as the crisis was overcome, the power to impose such regulations evaporated.¹⁴ Other decisions had emphasized the emergency nature of the general clause of section 91.¹⁵ The two decisions of 1937 now being reviewed made it finally clear that this general power was operative only in temporary and overwhelming emergencies such as war, pestilence or famine.¹⁶

The Canadian dilemma over social legislation was thus sharply outlined. The constitution forbids the Dominion to establish uniform labour legislation of general application and, despite the unrestricted taxing powers of the Dominion, the possibility of framing any contributory social insurance scheme of nation-wide extent which could be validly enacted by the Dominion, is open to the gravest doubt.

Temporary evils of great magnitude may be grappled with by Dominion legislation under the general clause of section 91 but an enduring and deep-rooted social malaise, which requires the mobilizing of efforts on a nation-wide scale to deal with it, is beyond the power of the Dominion unless it is comprised in the enumerated heads of section 91. Generally, therefore, the power to deal with these pressing social questions rests with the provinces. But this makes it very difficult to secure the uniformity of standards which are desirable in many kinds of social legislation. Moreover, the provinces are limited in their access to revenues by the financial settlement of 1867 (and in practice by Dominion taxation in the same fields) and many of them are unable to carry the financial burden involved.

Of course, these difficulties had been encountered in practice long before the Privy Council decisions of 1937. Over a period of twenty-five years, several attempts have been made to overcome them by the method of Dominion conditional grants of financial assistance to the provinces. In various matters where uniform governmental action was deemed desirable in the national interest, the Dominion has made grants available to the provinces for special purposes on condition that the province undertake the work and maintain certain standards, designed to secure a fair degree of uniformity across the country.¹⁷ The Dominion has tried to secure sufficient control over the administration of the particular activity by the provinces to enforce the maintenance of the desired standards. This has involved very substantial efforts in administrative co-operation between the provinces and the Dominion. The results obtained from this co-operation are far from reassuring.¹⁸ The experience gained from these efforts will be discussed later.

¹² *Attorney-General of Canada v. Attorney-General of Ontario*, [1937] A.C. 355.

¹³ *Fort Frances Pulp and Paper Company v. Manitoba Free Press*, [1923] A.C. 698.

¹⁴ *In re Board of Commerce Act*, [1923] 1 A.C. 191.

¹⁵ *E.g.*, see *Toronto Electric Commissioners v. Snider*, [1925] A.C. 398 at p. 412.

¹⁶ Under normal conditions, only a few matters of minor importance, not significant for present purposes, have been held to come within the scope of the general power in s. 91. For a list of these, see Plaxton, *Canadian Constitutional Decisions of the Judicial Committee, 1929-1939*, p. XXXII. (All important constitutional decisions in this period are included in this volume.)

¹⁷ For an account of these grants see Wilfrid Eggleston and C. T. Kraft, *Dominion-Provincial Subsidies and Grants* (mimeographed), pp. 35ff. The constitutional validity of such grants is not entirely beyond doubt. *Attorney-General of Canada v. Attorney-General of Ontario*, [1937] A.C. 355 at p. 366.

¹⁸ For a discussion of the working of the administrative relationships involved in these grants, see Appendix 7—J. A. Corry, *Difficulties of Divided Jurisdiction*, Ch. VI; cf. Eggleston and Kraft, *op. cit.*

The fifth Dominion enactment to be held *ultra vires* by the Privy Council in 1937 was the *Natural Products Marketing Act*. It provided for regulation of the marketing and distribution of natural products by a Dominion Marketing Board. The Board was given power, under certain conditions, to determine the time and place of and the agency for marketing as well as the quantity, quality and grade of any natural product which was to be allowed to be marketed at any time. The Act was to be applicable to a particular natural product only when the principal market for it lay outside the province of production or when some portion of it went into export trade. When these conditions were satisfied, the regulations contemplated by the Act were applicable to all marketing transactions in the particular product, including those which were finally completed within the province of production. In other words, the Act was applicable to some portion of purely intra-provincial trade as well as to interprovincial and export trade.

The Privy Council found this measure to be beyond the power of the Dominion Parliament because the federal power to regulate trade and commerce under section 91 (2) did not extend to the regulation of trading transactions completed within a single province.¹⁹ This ruling confirmed earlier decisions on the meaning of the phrase, "regulation of trade and commerce". Whatever its exact scope, it was confined to interprovincial and international aspects of trade. According to rulings of the Privy Council, it does not justify the regulation of the financial practices of insurance companies,²⁰ nor general regulation of the grain trade²¹ through a system of licences. It does not cover prohibition of trade combinations and regulation of the supply and price of the necessities of life.²² Nor do compulsory provisions for investigating industrial disputes come within its terms.²³

In each of these Dominion attempts at economic regulation just referred to, the common defect was that each involved an interference with trades and businesses carried on within a single province and was not applicable merely to interprovincial or international aspects of trade and commerce.

Although the exact scope of the phrase "regulation of trade and commerce" is not yet clear, it is settled that it does not cover the regulation of purely provincial trades, businesses and business transactions. Power to establish such regulations belongs exclusively to the provinces.²⁴ On the other hand, it is equally clear that the provinces have no power to regulate interprovincial and export trade.²⁵ The Privy Council ruling of 1937 holding the *Dominion Natural Products Marketing Act* invalid emphasized again the fact that the power to regulate economic life is divided between the provinces and the Dominion, and that neither one can encroach upon the sphere of the other.

It should be pointed out by way of caution, however, that the Dominion, relying on other heads of section 91, has a considerable power of economic regulation. It has some power of control over the operations of companies with Dominion charters which are, in substance, its own creatures and, therefore, in some degree, subject to its supervision. By use of its power to declare local works to be for the general advantage of Canada, it has been able to exercise effective control over the grain trade.²⁶ As was confirmed by the Privy Council in one of the references concerning the social legislation of 1935 which is not specifically discussed here, the Dominion Parliament, under its power to enact the criminal law, has power to prohibit economic practices (e.g. certain kinds of trade combinations), provided the courts are satisfied that Parliament has acted in good faith in stigmatizing them as criminal offences and is not "using the criminal law as a pretence or pretext" to encroach upon provincial powers.²⁷ Under other specific powers, the Dominion has extensive control over banks and monetary matters, bankruptcy, railway and air transportation, shipping and interprovincial communications.²⁸ In other fields and other circum-

¹⁹ *Shannon et al. v. Lower Mainland Dairy Products Board*, [1938] A.C. 708.

²⁰ *Lawson v. Interior Tree Fruit and Vegetable Committee*, [1931] 2 D.L.R. 193; *In re Grain Marketing Act*, [1931] 2 W.W.R. 146.

²¹ This power of the Dominion which is derived from the exception to s. 92 (10) was employed to declare all the grain elevators used in the western grain trade to be works for the general advantage of Canada. The validity of this use of the device has not yet been considered by the Privy Council but it is supported by the high authority of Duff, C.J., who suggested it as a means of establishing Dominion control over the grain trade. See *The King v. Eastern Terminal Elevator Co.*, (1923) S.C.R. 434 at p. 448.

²² It is difficult to state exactly the scope of the Dominion power to make criminal law. Compare *In re Board of Commerce Act*, [1922] 1 A.C. 191 with *Proprietary Articles Trade Association v. Attorney-General of Canada*, [1931] A.C. 310. The latter decision is confirmed by the Reference re section 498A of the Criminal Code, [1937] A.C. 368 and it is believed that the statement in the text sums up the law as accurately as it can be stated at present.

²³ The extent of Dominion power over these topics depends upon the enumerated heads of a. 91.

¹⁹ *Attorney-General of British Columbia v. Attorney-General of Canada*, [1937] A.C. 377.

²⁰ *Attorney-General of Canada v. Attorney-General of Alberta*, [1916] 1 A.C. 585; *Attorney-General of Quebec v. Attorney-General of Canada*, [1932] A.C. 41.

²¹ *Re v. Manitoba Grain Co.*, [1922] 2 W.W.R. 113; *The King v. Eastern Terminal Elevator Co.*, [1925] S.C.R. 434.

²² *In re Board of Commerce Act*, [1922] 1 A.C. 191.

²³ *Toronto Electric Commissioners v. Sneider*, [1925] A.C. 306.

stances, however, it cannot go beyond regulation of the interprovincial and international manifestations of business activity.

While the desirability of the sweeping kind of regulation contemplated by the *Natural Products Marketing Act* is the subject of considerable controversy, the pronouncement of its invalidity by the Privy Council confirmed earlier doubts about the validity of several much less drastic Dominion measures relating to marketing,²⁹ which were generally agreed to be desirable. Several Dominion statutes had set up compulsory grading legislation on a nation-wide scale for a variety of natural products. From time to time, most of the provinces had sought to cure any possible constitutional defects of these Dominion enactments by enabling legislation designed to authorize the Dominion to impose its grading regulations on purely provincial transactions.³⁰ In 1935 and 1936, several provincial Courts of Appeal held that this enabling provincial legislation, in the form in which it came before them, was invalid, being an unconstitutional delegation of power to the Dominion.³¹

The delegation of power by a province to the Dominion and vice versa would be a useful device for overcoming, in practice, the difficulties which arise from the division between the provinces and the Dominion of legislative power over many complex economic activities. Unified control and administration in the hands of a single government is sometimes desirable but it is very doubtful whether, as the constitution stands at present, the delegation of legislative power is constitutionally possible.³²

Such a power of delegation would give the constitution a flexibility which might be very desirable. With the present degree of economic integration on a national scale, it is extremely difficult for either the Dominion or a province to frame legislation which will deal separately and effectively with the local or with the interprovincial aspects of business activity, as the case may be. When natural products are assembled for national or international markets and the manufacturing and distributive trades operate on a nation-wide or international scale, most of the large important trades and businesses are engaged at the same moment in both intra-provincial and extra-pro-

vincial activities. These activities are so intertwined that it is difficult to isolate purely intra-provincial activities so as to apply provincial regulations to them and equally difficult to select the interprovincial activities and foreign activities which are subject solely to federal regulation.

For example, the grading of natural products, in order to serve its purpose, should be done when the product passes from the producer into the hands of the dealer, but it is frequently impossible at that stage to tell whether the particular lot of produce is destined for intra-provincial or for interprovincial or export trade and, therefore, impossible to say whether provincial or federal regulations should be applied. In the absence of a power to delegate legislative authority and control to a single government in such situations, the only alternative where comprehensive regulation seems desirable is a scheme of joint Dominion and provincial legislation and administration. For reasons which are noted later, such schemes have inherent weaknesses which can be avoided by delegation of legislative power to a single authority.³³

Several situations have arisen where regulation is admittedly necessary but the constitution divides the power of regulation between the provinces and the Dominion. The case of the marketing of natural products has already been noted. The fact that the ownership of inland fisheries goes with the public domain to the provinces while the Dominion has the ownership of the seacoast fisheries and the full power of regulation over all fisheries³⁴ has caused some confusion. The Dominion has power to enact compulsory legislation concerning industrial disputes in industries over which it has a comprehensive general power of regulation, such as interprovincial railways. The provinces have power generally to legislate respecting industrial disputes and, therefore, situations may arise where two or more governments are concerned in the settlement of a dispute.³⁵ In each of these cases, efforts have been made in the past to surmount the difficulties by delegation of power but they are now either embarrassed or being abandoned owing to the dubious constitutionality of the device.

²⁹ *Id.*, see *Re v. Collins*, [1936] 50 O.L.R. 453.

³⁰ For an account of the nature of this provincial legislation, see Appendix 7—J. A. Corry, *Difficulties of Divided Jurisdiction*, pp. 13-16.

³¹ *Re v. Eastensby*, [1935] 2 D.L.R. 788; *Re v. Brodeley*, [1936] 1 D.L.R. 578; *Re v. Thornby Traders Ltd.*, [1936] 1 D.L.R. 582.

³² For a discussion of the constitutional validity of the delegation of legislative power, see Appendix 7—J. A. Corry, *Difficulties of Divided Jurisdiction*, p. 27.

³³ See Book II, Sec. A, Ch. V, Pt. 2.

³⁴ *The Fisheries Case*, [1898] A.C. 700; *Attorney-General of British Columbia v. Attorney-General of Canada*, [1914] A.C. 153. The division of jurisdiction in the Province of Quebec is somewhat different from that in other provinces. See *Attorney-General of Canada v. Attorney-General of Quebec*, [1921] A.C. 412. For further discussion and recommendations, see Book II, Sec. A, Ch. IV, Pt. 2.

³⁵ For further discussion and recommendations, see Book II, Sec. A, Ch. II.

Power to regulate the financial practices of insurance companies does not belong exclusively either to the Dominion or to the provinces. The Dominion has power to regulate companies with a Dominion charter. The Dominion also exercises supervision over British and foreign insurance companies doing business in Canada. The constitutionality of this practice is not beyond doubt.³⁶ On the other hand, the provinces have the power to regulate the activities of all insurance companies carrying on business within the province.³⁷ As a result, separate and overlapping systems of Dominion and provincial supervision have grown up causing duplication of government machinery and unnecessary expense and inconvenience to insurance companies.³⁸

By way of summary then, the constitution as it stands today divides the power of regulating economic activity between the provinces and the Dominion. A great deal of the business activity of today is national in its scope and cannot be easily divided into intra-provincial and extra-provincial aspects for the purpose of regulation which may seem desirable. The delegation of legislative power by a province to the Dominion and vice versa, which would make possible a unified authority without any drastic amendments of the constitution increasing the power of the Dominion, is of doubtful constitutionality. Furthermore, the present division of legislative power under the constitution throws the main burden of modern social legislation on the provinces. The support of such legislation has become one of the heaviest financial charges which governments are obliged to meet. The division of taxing powers which gives the Dominion unlimited access to sources of revenue and restricts the provinces to a limited number of sources is discussed elsewhere.³⁹ The scope of the provincial power of taxation as explained by Privy Council must be considered briefly here.

Interpretation of Provincial Taxing Powers

Section 92 (2) gives the provinces power to levy "direct taxation within the province". Also, under section 92 (9) "shop, saloon, tavern, auctioneer and other licences" may be imposed for the purpose

of raising revenue. The scope of section 92 (9) is not yet entirely clear. It is not entirely certain whether indirect as well as direct taxation is authorized under this head nor whether licences may be imposed on any kind of business activity or only on a limited genus of which those specifically mentioned are examples.⁴⁰ It is not highly important for purposes of this chapter because the great source of provincial revenues is direct taxation under section 92 (2). But if our recommendations (made in Book II) for the transfer of taxes are implemented, it would be very important that the scope of the power to raise revenue by licence fees should be clearly defined.

In an earlier chapter the criterion of direct taxation adopted by the Privy Council was discussed.⁴¹ The rule laid down in the case of *Bank of Toronto v. Lambe* in 1887 that "a direct tax is one which is demanded from the very persons who it is intended or desired should pay it" has been explained and amplified in later decisions. In substance, it has been held that a provincial legislature, in levying a tax, must intend the natural consequences of its action and, therefore, "it is the nature and general tendency of the tax and not its incidence in particular or special cases",⁴² which determine whether it is a direct tax within the power of the provinces to levy. Accordingly, if in the normal course of events, the burden of the tax is likely to be shifted to others by the person who is required to pay it, the tax is indirect.

The result of the application of this rule has been almost entirely to prevent provincial taxation on industrial production and wholesale turnover and to limit the productivity of provincial taxation by restricting it, in the main, to levies on the ultimate consumer. A percentage tax on the gross revenues of mining enterprises is an indirect tax.⁴³ So is a tax payable by the first purchasers of fuel-oil after its manufacture or importation.⁴⁴ So also is a tax levied on sales of grain for future delivery.⁴⁵ On the other hand, a tax payable by the consumer of fuel-oil according to the quantity consumed is a direct tax.⁴⁶ Thus the familiar

⁴⁰ See Kennedy and Wells, *Law of the Taxing Power in Canada*, Chapters V and VI.

⁴¹ See pp. 44-46.

⁴² *City of Halifax v. Fairbanks Estate*, [1928] A.C. 117 at p. 128.

⁴³ *The King v. Caledonian Collieries Ltd.*, [1928] A.C. 358.

⁴⁴ *Attorney-General of British Columbia v. Canadian Pacific Railway Co.*, [1927] A.C. 934.

⁴⁵ *Attorney-General of Manitoba v. Attorney-General of Canada*, [1925] A.C. 561.

⁴⁶ *Attorney-General of British Columbia v. Kingcome Navigation Co.*, [1934] A.C. 45.

³⁶ Dominion legislation affecting these companies was held *ultra vires* by the Privy Council in 1932. See *Attorney-General of Quebec v. Attorney-General of Canada* [1932] A.C. 41. Following this decision, Parliament amended the legislation and the courts have not yet passed on it in its amended form.

³⁷ *Attorney-General of Ontario v. Reciprocal Insurers*, [1924] A.C. 328.

³⁸ See Appendix 7—J. A. Corry, *Difficulties of Divided Jurisdiction*, Chapter II. For further discussion and recommendations, see Book II, Sec. A, Ch. IV, Pt. 4.

³⁹ See pp. 40-46.

gasoline tax and the retail sales taxes found in some provinces are direct taxes within the power of the provinces because, by making the retailer the agent of the government for purposes of collection, they are deemed to be levied directly on the consumer who cannot naturally and easily shift the burden of them to others.

Fortunately for the yield of provincial taxation, the provinces have been able to go beyond taxes on consumption in the corporation taxes and succession duties. The validity of a corporation tax as a direct tax was upheld in 1887.⁴⁷ A province has power to levy a tax on any corporation which is exercising its powers within the province.⁴⁸ The so-called succession duties which, in most provinces, are, in part, probate duties levied on *property* as such and in part, legacy duties levied on the *transmission* of property from the deceased to beneficiaries are validly imposed by the provinces under certain conditions.

A probate duty is a direct tax but the provinces, being restricted to taxation "within the province", can levy only on that portion of the property of the deceased which is found within the province.⁴⁹ A legacy tax, or succession duty proper, satisfies the test of "direct taxation within the province" when levied on beneficiaries domiciled or resident in the province in respect of the transmission of property to them by virtue of the law of the province. Under certain conditions, the province, by taxing the transmission of the property to a beneficiary domiciled or resident within the province rather than the property itself, is able to impose, in substance, a tax upon "movable" property situated outside the province.⁵⁰

Under certain circumstances, provincial succession duty can reach property in another province. With two exceptions, all the provinces do extend their succession duties to property in other provinces. At the same time, they all levy a probate duty on property situated in the province. Thus estates of deceased persons are subjected to the inequity of double tax whenever "movable" property belonging to the estate is found in more than one province.

⁴⁷ *Bank of Toronto v. Lamb*, (1887) 12 A.C. 575.

⁴⁸ Kennedy and Wells, *Loss of the Taxing Power in Canada*, pp. 66-78.

⁴⁹ *Ree v. Lovitt*, [1912] A.C. 212.

⁵⁰ An exact statement of the constitutional power of the provinces to levy succession (i.e. legacy) duties would require a preliminary examination of other branches of the law and a lengthy discussion which is not necessary for present purposes. The authoritative statement of the law is to be found in *Provincial Treasurer of Alberta v. Kerr*, [1933] A.C. 710. See Falconbridge, "Administration and Succession in the Conflict of Laws", [1934] 12 *Canadian Bar Review*, 67 at pp. 70-79 for a clear statement of the position.

Long efforts by the provinces to eliminate double taxation of estates by agreement have broken down completely under the stress of the depression.

Disallowance of Provincial Legislation

Before concluding this review of the constitution as it works today, it is necessary to refer to the present status of the federal power of disallowing provincial statutes. Although the scope of this power given by the British North America Act is legally unlimited, except as to time, it has been recognized from the beginning that it should be used with circumspection and in accordance with some guiding principles. The principles relied on by the Dominion Government in the exercise of disallowance have varied from time to time and it is, therefore, impossible to state them with precision. There has been no such consistent and unbroken practice as would be necessary to establish a constitutional, or conventional, limitation on the exercise of the power. There is reason for thinking that it will not again be used as freely as it was during the first thirty years of Confederation but this cannot be stated with finality.

As we have remarked earlier,⁵¹ the Dominion made very extensive use of the power of disallowance between 1867 and 1896. Not only was provincial legislation disallowed on the grounds that it was *ultra vires* or in conflict with Imperial or Dominion interests or policies. Provincial legislation might also be struck down on a ground which had great potential scope, namely, that it was inequitable and unjust. From 1896 to 1911, the Dominion Government consistently disavowed this last ground as a sufficient reason for exercise of the power. After 1911, there was a tendency to reaffirm the propriety of disallowing provincial legislation which the Dominion Government thought to be inequitable and unjust but this ground was actually relied upon in two cases only, arising in 1918 and 1922.

The power of disallowance was in complete abeyance from 1924 until 1937 when it was used against a number of Alberta statutes. Again in 1938 and in 1939, Alberta legislation was disallowed. Apart from showing that the power of disallowance has not become generally obsolete, the recent use of it does not throw any new light on its scope. Most of the eight Alberta statutes disallowed since 1937 were invasions of the federal field of legislation, conflicting with the interests and policies of the Dominion. However, among the reasons given for disallowance of two of these statutes, specific

⁵¹ See p. 49.

reference was made to the injustice of the confiscations which they proposed and to their discriminatory character.

Thus it is quite impossible to regard disallowance on grounds of inequity and injustice as obsolete.⁵² It is true that in declining to disallow the so-called Padlock Law of Quebec in 1938 the Government disclaimed any intention to review the policy of provincial legislatures acting within their own field of competence. It is also true that in the Alberta cases, the distinct ground of interference with Dominion policy and interests was available in each case and relied on. But the only inference to be drawn from the recital of the unjust, confiscatory and discriminatory character of legislation is that these qualities are relevant to the use of the power. Nevertheless, the whole trend indicates a lessening use of the power. Up to 1900, 72 provincial acts were disallowed while only 35 have been disallowed since that time.⁵³ It seems unlikely that disallowance on grounds of inequity and injustice will ever resume the importance it had prior to 1896.

It must be remembered also that in 1867, the world had had little experience of widespread democratic suffrage and much thought was expended on finding ways to prevent legislatures from abusing their powers. In that temper of affairs, whatever may have been the special reasons for inserting the power in the Canadian constitution, there is little wonder that it was extensively exercised. As time went on, confidence in the self-restraint of democratic legislatures increased and willingness to accept their measures with resignation also grew. In other words, the principle of legislative sovereignty is more fully accepted now than it was in 1867. The decisions of the Privy Council that the provincial legislatures are sovereign in their own sphere have operated to secure for them also the benefit of this acceptance. Consequently, the trend towards a narrower use of the power is likely to be sustained, although it is impossible to say that a different policy would not be adopted in special circumstances.

Difficulties of Divided Jurisdiction

At two points in particular, the division of legislative powers has led to attempts at close co-operation between the Dominion and the provinces. First, where the financial resources of the

provincial governments are not commensurate with their legislative powers and consequent responsibilities for maintaining desired social services, the Dominion has made money grants to the provinces to assist in the maintenance of such services. Hoping to ensure the nation-wide maintenance of certain minimum standards in the assisted services, the Dominion imposes certain conditions on the grant and conducts a periodic inspection of the service given by the province. Hoping to hold the provinces to careful stewardship of funds which they do not themselves raise, the Dominion supplements its inspection activities with a detailed audit of provincial expenditures. Agreements as to the conditions on which the provinces are to undertake and the Dominion is to assist such services must be made at the political level. Federal officials are constantly investigating specific activities of provincial officials at the administrative level. Disagreements at either level may prejudice Dominion-provincial relations.

Second, in the field of economic regulation, where legislative power is divided, the Dominion and the provinces have made some attempts at co-operation, particularly in establishing nation-wide regulations for the grading of agricultural products. At first a device was used which, in substance, amounted to a delegation of power by the provinces to the Dominion enabling the Dominion to impose grading regulations on all transactions. However, after doubts arose as to the constitutionality of this practice, the provinces began to meet the problem by enacting the Dominion grades and regulations as provincial legislation and appointing Dominion inspectors and officials to act as provincial officials. Whereas the device of delegation was a very simple arrangement for unifying the administration of grading regulations in the hands of a single government, the new method involves the continuous co-operation of ten legislatures and ten governments in joint administration, making necessary a higher degree of sustained harmony and agreement.

These co-operative ventures are opening a new chapter in Dominion-provincial relations. A certain minimum of co-operation is always necessary if separate governments are to share in governing the same area and the same people. The original purpose of the constitution was to set up a sharp division of powers enabling each government to manage separately without interference the affairs allotted to it and to reduce all intergovernmental difficulties to a question of power and legal competence. Because different governments were

⁵² In the reference *re Power of Disallowance and Power of Reservation*, [1939] 3 D.L.R. 8, the Supreme Court of Canada held that the only limitation was the time limit fixed by the British North America Act.

⁵³ *Memorandum on Dominion Power of Disallowance of Provincial Legislation*, Department of Justice, Ottawa, 1937.

likely to disagree from time to time about the extent of their respective powers, such questions are always referred to the courts for their final determination as independent and impartial bodies. The co-operation required between governments in these circumstances was mainly of a negative character; each should abstain from interfering with the others.

But Dominion and provincial governments are now embarked on the joint administration of projects which require positive and constructive co-operation if they are to be carried out efficiently. Two separate governments, neither one of which has any authority over the other, must agree on objectives, on the means of reaching them, and on the daily application of these means to new situations. However, there are always a number of issues on which the interests of the Dominion and those of the separate provinces do not run side by side. These differences in interest lead to disagreements which cannot be solved by appeals to the courts because they do not involve questions of formal constitutional power at all. They are disagreements about matters which the constitution intended that the appropriate government should handle separately in its own way.

Accordingly, if the co-operative projects are to be continued, the governments involved must be their own arbitrators. Arbitration conducted solely by the interested parties leads to delay and sometimes to deadlock which is ruinous to administrative efficiency. It always leads in the end to a compromise. While compromise is inherent in the political process, it is rarely conducive to good administration. The evolution of political policies within the framework of the constitution is leading to joint activity between the Dominion and the provinces. This contrasts sharply with the original conception of federalism as a clear-cut division of powers to be exercised separately, and experience indicates that it is injurious both to sound public finance and to efficient administration. The problems raised by joint administration of activities where jurisdiction is divided between the provinces and Dominion may now be pointed out. The first step in any scheme of co-operation must generally be taken by the legislatures concerned. As indicated above, the divided legislative powers over the subject-matter in question could be pooled by one legislature delegating its share of power to the other if the constitutionality of such an expedient had not been rendered doubtful by the courts.⁵⁴ If it were constitutionally possible and

the province or Dominion, as the case may be, were willing to delegate its powers in the specific instance, the act of delegation would complete the co-operation required. The legislature receiving the powers could then establish its regulations and provide for their enforcement just as if the entire matter had originally been within its jurisdiction. In such a case, no joint administration by province and Dominion would be involved and as long as the legislature delegating its powers was satisfied with the results obtained, through vicarious use of its powers, no further action by it would be required.

In the past, the Dominion and provincial legislatures have had no serious difficulty in agreeing on this kind of co-operation. Nation-wide schemes for the compulsory grading of natural products under the administration of the Dominion Government were set up and the provinces purported to extend the Dominion Industrial Disputes Investigation Act to disputes entirely within the jurisdiction of the provinces by essentially similar devices. The administration of the legislation was placed in the hands of a single government⁵⁵ and the difficulty arising out of the division of legislative power over the subject matter was surmounted. The constitutionality of this procedure was, however, challenged by the courts in 1935. As a result, the provinces have begun to abandon this method in favour of a more complicated one which escapes the constitutional difficulty but which involves joint administration. The new device requires that the province should enact legislation in substantially identical terms with that of the Dominion but covering intra-provincial as distinct from inter-provincial and export transactions. To be specific, in legislation providing for the compulsory grading of natural products, the province enacts the Dominion grades and regulations for enforcement and then appoints the Dominion graders and inspectors as provincial officials to enforce the provincial as well as the federal legislation.⁵⁶

Close and continuous co-operation is necessary for success under this device. Any needed revision in the detailed regulations or definition of grades must be made by both the provincial and Dominion authorities concerned. They must be able to agree on the need for change and the exact nature of the change required. Moreover, the graders and

⁵⁴ *Rea v. Zaslavsky*, [1935] 3 D.L.R. 788.

⁵⁵ The extent and nature of these co-operative schemes are discussed in Appendix 7—J. A. Corry, *Difficulties of Divided Jurisdiction*, pp. 12-18.

⁵⁶ *Ibid.*, pp. 20-21.

inspectors are now subject to the control of two masters, the Dominion and provincial departments concerned. The intention, of course, is to leave the initiative and the general control of administration of grading legislation to the Dominion and thus far in the limited experience of the new device, this has been the practice. However, it can only be a matter of time until it is discovered that the principles of responsible government are being flouted when provincial legislation is administered by officials who get all their instructions from Ottawa. Administration will then become joint in substance as well as in form.⁵⁷

Thus far, activities jointly administered by the Dominion and a province have not been of any significant magnitude or duration in Canada. As already remarked, however, the present division of legislative power and the present trend towards greater governmental regulation are rapidly leading in that direction. Although direct Canadian experience of joint administration is not available for assessing its probable efficiency, an appeal can be made to twenty years of experience in the administration of conditional grants in Canada. It has already been pointed out that, in the conditional grants made by the Dominion to the provinces to assist specific services, the Dominion attempts, by supervision and inspection of the provincial administration, to ensure that the grant is being properly applied to the purposes for which it was given. This involves a form of co-operation approaching joint administration and raises most of the problems involved in it. Before considering the manner in which conditional grants have worked in Canada, it is important to state some general considerations bearing upon all co-operative efforts in administration by separate governments.

It is clear that failure of Dominion and provincial government departments to pull together in such co-operative ventures will have disastrous effects upon administration. The purpose of all administration, whether in government departments or in private enterprise, is to get something done, to unify the efforts of the personnel in reaching objectives laid down beforehand. One of the principal differences between government and business is that the objectives and policy of government, in democratic states, at any rate, are generally arrived at as a result of bargaining and compromise among a wide variety of interests concerned. But once a policy is agreed upon, it is a maxim of all

good administration that concerted effort in pursuit of the policy should not be frustrated by a multitude of counsel on the best means of arriving at it.

In business, unity of effort is secured by having a single manager responsible for administration as a whole. The Constitution of the United States aimed to reach the same result by concentrating all executive authority in the hands of the President. In the cabinet system of government, the conventions requiring unanimity and imposing collective responsibility are designed to secure a similar co-ordination of all administrative action.

Where the Dominion and the provinces co-operate in the execution of a single policy, there is no single authority which can impose its will and decide what daily action shall be taken in pursuit of objectives. The Dominion and the provinces occupy exclusive spheres of power in which no one can over-ride the others. If unity and harmony of administration are to be maintained, it must be through voluntary agreement between Dominion and provincial personnel on the best means of advancing the policy. And this agreement must be reached without delay and without serious compromise watering down the vigour of the measures employed.

It is one thing to get a legislature willing, at a single moment of time, to delegate some portion of its powers. Once the act of delegation is complete, it is not likely to reconsider its action until administration by the authority to whom the power was delegated becomes highly unsatisfactory. It is a quite different matter, however, to get sustained unanimity on the minutiae of administration from day to day. There are two main reasons for thinking it likely to break down from time to time.

It is no criticism of higher government officials to say that they generally like to extend the sphere of their authority. Like everyone else, the energetic official must try to express his personality in his work. He must try to prove the correctness of his ideas by putting them into practice and, in this way, prove himself to his superiors. Quite naturally, he wants credit for successful administration and he, therefore, cannot acquiesce in methods and practices which he thinks are prejudicial to it. In the nature of things, there are forces making for rivalry between Dominion and provincial officials who are co-operating in joint administration. Honest differences of opinion quite unconnected with personal ambitions are often sufficient to bring them into disagreement. Sooner or later, the incompatibility of their ideas or their ambitions are likely to lead to different views on

⁵⁷ A number of the difficulties which may be expected to attend the use of this device are set out in Corry, *op. cit.*, pp. 22-30.

administration. Such rivalries and differences of opinion have prejudiced Dominion-provincial co-operation in many instances in the past. They are to be found between officials within a single government where it is only the unified control of administration in the hands of the cabinet which prevents them from seriously impeding administration. Officials testify to their existence by saying that success in Dominion-provincial co-operation in administration depends entirely upon "personalities".⁵⁹

Secondly, in joint administration the officials in the provincial department concerned are responsible through the minister to the provincial legislature, while the federal department is likewise responsible to Parliament. Politics and administration are closely linked by the cabinet system. The Government of the Dominion and the government of a province, as is well known, may be at odds over some question of policy. On occasion there are genuine conflicts of interest between the Dominion as a whole and one or more provinces. Moreover, where active administration affects the interests of particular persons or groups, representations are made by them to the government of the day, which is sometimes constrained, as a result, to intervene in administration on political grounds. Thus there will be a tendency for joint administration to get entangled in political issues. Where both Dominion and provincial politicians have access to administration, there will be constant danger of Dominion-provincial political friction being transmitted to areas of joint administration.⁶⁰

There is no occasion to be critical of political differences between the Dominion and a particular province. It is the duty of a provincial legislature and government to pursue the interests of the province as they conceive them to be, just as it is the duty of Parliament and the Dominion Government to push forward what they believe to be the national interest. These apparent conflicts of interest can scarcely be avoided. But they should be fought out in the political arena and not permitted to engage one another in the sphere of administration where they will destroy vigour and efficiency.

In the United States the cabinet system of government is not used and members of the legislature cannot intervene in daily administration. Thus administration is, in a considerable measure, insulated from politics. Accordingly, joint administration of projects by federal and state governments escapes one of the serious difficulties to

which it is exposed in Canada. It is dangerous therefore to argue from experience in this field in the United States.

These general considerations do not apply with equal force to all kinds of joint activity. In activities which can be largely reduced to a number of routine operations and which do not have to wrestle constantly with new situations and new problems, the danger of differences between officials is considerably less. The same is true of activities which consist mainly in the application of scientific standards. To some extent, the discipline of science compensates for the lack of a discipline imposed by a single superior and the recondit nature of the problems which arise tends to withdraw the activity from the intrusion of political differences between the provinces and the Dominion.

Limitations of Conditional Grants

On the whole, however, these general considerations suggest that joint administration by Dominion and provinces is not likely to be very satisfactory. The history of the administration of conditional grants in Canada points in the same direction. From 1912 on, the Dominion has made grants of money to the provinces for specific purposes on specified conditions. Grants for assisting agricultural instruction, highway development, technical education and control of venereal disease have expired and have not been renewed. Grants for employment offices, old age pensions and unemployment relief are still being made. The activities being assisted are in each case within the constitutional power of the provinces and accordingly they are administered primarily by the provinces. As indicated earlier, the Dominion agrees to give financial aid to a provincial service provided the province spends equivalent or specified sums on it and maintains certain standards in the service rendered. Thus it is necessary for the Dominion and the province to agree upon the standard and the means of reaching it. The agreement is embodied in a set of regulations which are to govern administration and the claim of the province to Dominion financial assistance depends on the observance of these regulations. In an attempt to ensure careful application and substantial observance of the regulations, the Dominion Government audits provincial expenditures on the assisted service and, where feasible, measures performance against the standard by supervision and inspection.⁶¹

⁵⁹ See Corry, *op. cit.*, pp. 9-10.

⁶⁰ *Ibid.*, pp. 17-18, 34-35.

⁶¹ See Corry, *op. cit.*, pp. 25-36, for a discussion of the administration of conditional grants.

Such administration is, in a sense, joint. Dominion auditors and inspectors check provincial accounts and the actions of provincial officials, while provincial officials are obliged to get the approval of federal officials if there is to be no interruption in payments of the federal grant. Disagreements between the two sets of officials involved cause delay and confusion and lower the efficiency of administration. We are convinced that, on the whole, the administration of the services assisted by these conditional grants has fallen far short of reasonably good administration. The basic reasons for this failure are the two set out above in general criticism of joint administration.

To decide whether particular payments have been properly made or whether provincial performance comes up to the agreed standard, it is necessary to interpret the regulations which define the conditions on which federal assistance is granted. Dominion and provincial officials frequently disagree about the meaning of the regulations. General rules are never entirely clear in their application to particular cases and most of the disagreements are genuine honest differences of opinion as to how the activity should be carried on in cases where the regulations are not entirely clear. It is true that the disagreements arise in a relatively few cases but since there is no single superior authority to resolve them, they are enough to cause delay, and may generate friction which spreads through the administration, and generally reduces efficiency.

The difficulty is that in many of the activities assisted by conditional grants it is impossible to find a clear-cut standard which can be applied automatically in measuring performance. Really objective criteria are hard to find in human affairs and where the measuring-rod cannot be applied automatically, it leaves room for difference of opinion.⁶² It is inevitable that federal inspecting and auditing officials should be primarily concerned with protecting the Dominion treasury while provincial officials engaged in active administration of the service are concerned with seeing that it meets what they conceive to be the needs for which it was established. Where there is room for difference of opinion, this difference in interest and purpose causes disagreements to emerge.

Federal officials cannot insist directly upon their interpretation of the regulations by giving orders to provincial officials in the field. Provincial officials must take their orders from the provincial

government and not from federal auditors and inspectors. Thus disagreements in the field are referred back to higher officials and ministers in Ottawa and in the provincial capitals, and questions of administration become the subject of diplomatic interchange between governments, involving long delays in their settlement.⁶³

When administrative questions rise to the political level, they tend to become entangled in political issues and to be treated as such. Nowadays Dominion and provincial policy impinge upon one another at many points. When, as a result of this fact, sharp differences emerge between the Dominion and a province, there is grave danger that the difficulties of joint administration will be intensified. The intrusion of politics in administration is always unfortunate but it is doubly so when a single government activity or service is disturbed by both federal and provincial politics.

In pointing generally to the difficulties in the administration of conditional grants, there is danger of creating false impressions. It must be emphasized that the exasperations noted are not found in all provinces nor at all times. If they were, conditional grants would never have survived their launching. But they occur with sufficient frequency to cause waste, friction and delay. Nor are they due to the perversity of officials and politicians. The federal scheme of government was devised precisely because of the lack of complete identity of interest between the whole and the component parts. Where differences of interest exist they become manifest simply through officials and politicians doing their duty. If these differences cut across fields of co-operative activity, they inevitably have a prejudicial effect.

Those who favour conditional grants as a means of overcoming constitutional difficulties are aware of the objection frequently made that governments which spend public money ought to be fixed with full responsibility of raising it. They argue that this objection is overcome and adequate control over provincial administration secured in two ways. In the first place, the grant is made for a particular purpose and the Dominion can define exactly what that purpose is. Then by supervision and inspection, it can determine whether provincial administration complies with the terms of the grant. If not, disallowances and deductions from the grant can be made as a penalty and a warning for the future. Secondly, if this sanction is not effective, the entire grant may be withheld until defects are remedied.

⁶² *Ibid.*, pp. 31-33.

⁶³ *Ibid.*, p. 33.

This argument ignores certain stubborn difficulties. In the first place, we have already pointed out that in many of the services assisted by federal grants, it is impossible to devise exact standards for measuring performance. Opinions differ as to what amounts to an earning of the grant and disputes arise. Federal auditors may disallow particular provincial expenditures as not being authorized by the regulations. Because there is generally room for difference of opinion, the province does not normally acquiesce in such action. In resisting a disallowance which it considers unfair, the province feels justified in bringing pressure on the Dominion. As the province is in full control of administration, there are generally a variety of expedients which it can adopt to inconvenience or prejudice the Dominion. Thus the Dominion is obliged to be very chary of disallowing expenditures except in very flagrant cases which, of course, are rare.⁶⁴

Moreover, in most cases, federal audit of provincial expenditures cannot go to the root of the activity. To determine independently the correctness of all provincial expenditures on an aided activity, it would be necessary to duplicate provincial field staffs. Such duplication of staff cannot, of course, be contemplated and federal audit is generally confined to a review of the documents and vouchers on file. Occasional test investigations by way of sampling are made and complaints of serious abuses investigated. We do not suggest that there is any need to inquire into the honesty of provincial administration but there may be occasions when its vigilance in these assisted activities is not as rigorous as if the province itself raised all the funds expended on them. In any case, federal audit and supervision cannot go to the root of these activities.⁶⁵

Secondly, the power of the Dominion to withdraw the grant from a province which fails to conduct its administration in accordance with the conditions imposed on the grant can rarely be exercised in practice. The Dominion assists particular provincial services because they further some important

national interest. Withdrawal of the grant to discipline a province must be at the expense of the national interest in question. Furthermore, it is a very serious matter to say that a provincial administration is so bad that assistance must be withdrawn. Obviously no Dominion Government could come to that conclusion about a provincial government of its own political stripe. And a Dominion Government would scarcely dare to withdraw a grant from a provincial government of a different political stripe because of repercussions in the province affected.⁶⁶

Thus the Dominion must always hesitate long before withdrawing a grant. The provinces know this and they are not seriously impressed by threats of such action. The power to withdraw the grant is not an effective sanction except against the most flagrant of abuses. Experience shows that where flagrant abuses have been brought to light, the province in question has hastened to correct them. In the prosaic but much more common cases, where administration is hampered by honest and reasonable differences of opinion, withdrawal of the grant as a means of resolving such differences is out of the question.

On these grounds we are satisfied that, for permanent purposes, the conditional grant, as it works under Canadian conditions, is an inherently unsatisfactory device. It may be used in some special cases and for some limited purposes, as we shall indicate later.⁶⁷ But in most activities we believe it to be more costly than if the service in question were financed by a single government. It unquestionably leads to delay and to periodic friction between Dominion and provincial governments.

The experience with conditional grants leads us to doubt whether joint administration of activities by the Dominion and a province is ever a satisfactory way of surmounting constitutional difficulties. Where legislative power over a particular subject matter is divided, it is ordinarily desirable that these powers should be pooled under the control of a single government in order to secure unified effort in administration.

⁶⁴ See *CORTY, op. cit.*, pp. 34-35.

⁶⁵ *Ibid.*, 29-31.

⁶⁶ *Ibid.*, pp. 34-35.

⁶⁷ See Book II, Sect. A, Chaps. I and III; Sect. B, Chap. V.