HOUSE OF COMMONS
CANADA

THE GOODS ON SERVICES

Report of the Standing Committee on Industry, Science and Technology

James Rajotte, M.P.
Chair

JUNE 2008

39th PARLIAMENT, 2nd SESSION

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THE STANDING COMMITTEE ON

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has the honour to present its

SECOND REPORT

Pursuant to its mandate under Standing Order 108(2) and the motion adopted by the Committee on November 20, 2007, your Committee has undertaken a study of a Review of Canada's Service Sector and has agreed to report the following:

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CHAIR'S FOREWORD

Canada's services sector is a vital component of our economy. As services provision has grown far more rapidly and consistently than that of goods throughout the past five decades, the shares of the services sector in total economic activity and employment have been increasing steadily over time. Indeed, while services output accounted for 58% of Canada's gross domestic product in 1975, it accounts for almost 70% today. Moreover, in 2007, the Canadian services sector provided employment for about 12.9 million people, accounting for more than 75% of employment and more than 90% of job creation since the worldwide "commodities boom" began in late 2002. All in all, these developments signal that Canada's economy has been undergoing profound, long-term structural change away from goods-producing activities and towards services, and it is incumbent upon public policy-makers to keep abreast and adapt their policies, strategies and programs to accommodate this different economic structure.

Although the sector has enjoyed tremendous growth in recent years, Canada's services sector is not without its set of challenges. The sector, as a whole, faces and will increasingly face a labour skills shortage as Canada's population ages, the rate of retirement increases, and the labour force shrinks. And certain sub-sectors face industry-specific challenges, such as the tourism and the hospitality industries (e.g., tour operators, hoteliers, convention centres, restaurants and special events) that are striving to cope in a very competitive market that has been struck by a number of political and business developments, including the high value of the Canadian dollar vis-à-vis the world's major currencies, high fuel prices, lengthy wait times at the border, and confusion surrounding passport requirements.

The Committee has completed an intensive study of the challenges facing the services sector. It began its hearings in November 2007, and engaged 60 witnesses representing many facets of the services sector. The Committee's final report reflects a wide perspective on the opportunities and challenges facing the services sector. The report offers specific recommendations to the Government of Canada on how it can help the sector adapt to the challenges it is facing. The Committee believes that the Government of Canada should implement its recommendations in a timely fashion.

I would like to thank all of the witnesses who have appeared before the Committee for their presentations and submissions. I also thank the members of the Committee and our committee staff for their hard work on this study.

James Rajotte, M.P.
Chair

INTRODUCTION

In November 2007, the House of Commons Standing Committee on Industry, Science and Technology (hereinafter the "Committee") began its hearings on the current state of the Canadian services sector. The Committee's mandate was to review the strengths of this sector, the challenges facing this sector, this sector's impact on Canada's economy and employment levels, and average salaries across this sector. Finally, the Committee was to study the role of the Government of Canada in strengthening the services sector.

This final report provides the Government of Canada with an overview of Canada's economy, highlighting recent structural changes arising from a worldwide "commodities boom" and, in turn, the consequent rapidly rising Canadian dollar. The worldwide "commodities boom", with its attendant high energy and industrial commodity prices, and the integration of China and other "emerging economies" into the world trading system, with the resultant increased competition placing additional restraints on price increases of domestic industrial and consumer goods, has led to an improved terms of trade for Canada. Foreign investors have also taken a renewed interest in Canada as an investment destination. As a result, wealth has been on the rise in Canada, and the economy has been expanding at breakneck speed for the past five years. This economic growth has been widespread throughout the Canadian economy, services-producing and goods-producing sectors alike, except for Canadian-dollar-sensitive industries such as manufacturing and tourism. In turn, employment across Canada has been growing; job creation has been spectacular; and both Canada's employment rate and unemployment rate have respectively set a 33-year high/low in the process.

Services in Canada span both the business and non-business (e.g., public and volunteer) sectors and, with annual growth in the services sector running about a half percentage point higher than the growth rate of the overall economy for the past five years, services have grown to account for almost 70% of economic activity in Canada. In 2007, the Canadian services sector provided employment for about 12.9 million people, accounting for more than 75% of employment and more than 90% of job creation since the "commodities boom" began in late 2002.

This study focused on the challenges that specific sub-sectors or industries are facing and the responses they have been taking to overcome these challenges. The industries included were:

- Financial services;
- Real estate, rental and leasing;
- Professional services;

- Healthcare;
- Retail trade;
- Food services;
- Travel and tourism;
- Transportation;
- Information and communications technologies;
- Culture;
- Gaming.

By far the most common challenge cited by virtually all industry representatives was the current and future labour/skills shortage, but many other industry-specific challenges were identified.

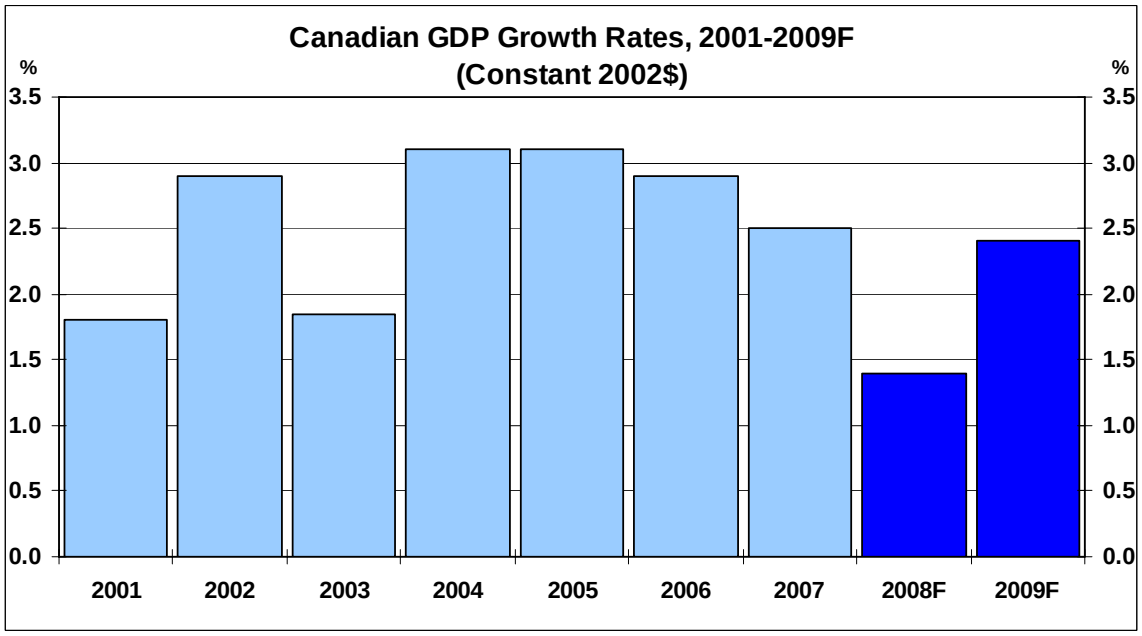
Finally, the Committee assessed all of the recommendations suggested by witnesses and then decided on a number of fiscal and non-fiscal measures. These measures form a body of recommendations to the Government of Canada on how it can help the Canadian services sector adapt to the challenges it faces. The Committee is convinced that the adoption and implementation of these recommendations will assist the services sector in making its maximum contribution to the Canadian economy.

CHAPTER 1
OVERVIEW OF THE CANADIAN ECONOMY

ECONOMIC PERFORMANCE

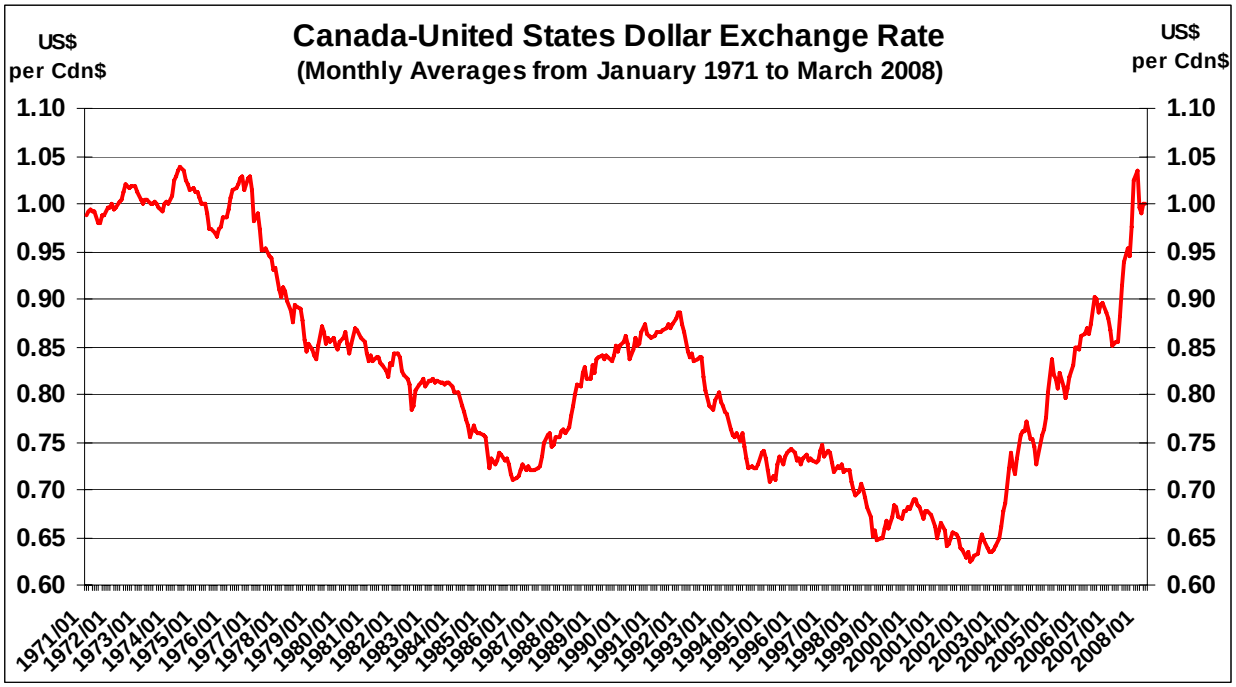
The Canadian economy has enjoyed robust growth over the past several years. Canadian real GDP — that is, Canada's nominal gross domestic product (GDP) discounted to account for price inflation — grew in five of the past six years, averaging almost 3% per annum in this period (see Figure 1). There are a number of reasons behind this strong economic performance — not the least of which has been resilient domestic demand — but probably the most important and surprising factor has been rapid world economic expansion since 2003, particularly buoyant in China, India and Southeast Asia. According to Consensus Economics, world real economic growth has averaged about 3.5% per annum between 2003 and 2007, but in these above-mentioned Asian countries real economic growth has been more than double that of the world average. At the centre of this stellar performance has been the Asian demand for industrial commodities — markets for which Canada is well suited to serve and commodities in which Canada possesses a comparative advantage, particularly in terms of energy and base metal products.

Figure 1



Source: Bank of Canada, Monetary Policy Report Update, April 2008.

Figure 2



Source: Bank of Canada, http://www.bankofcanada.ca/en/rates/can_us_lookup.html.

Without a doubt "Emerging Economies" such as China and India are a significant source of demand for industrial commodities and considerably higher Canadian commodity export prices, but they are also proving to be an increasing source of competition in a number of industrial and consumer goods. Indeed, substantially reduced prices for Canadian merchandise imports originating increasingly from Asia, which have acted as a check on rising domestic product prices, have been the most obvious and enduring economic impact on Canadian markets of integrating these "emerging economies" in the world trading system. As a result, Canada's terms of trade — that is, the ratio of Canadian export-to-import prices — has improved markedly in this period,[1] which has in turn led to a rapid and substantial appreciation of the Canadian dollar against many currencies, most particularly the U.S. dollar. Furthermore, Canada's much improved terms of trade appears to have sparked international investors' interest in Canada. Net foreign direct investment (FDI) flows, which had been mostly outbound rather than inbound to Canada in the last two decades of the 20th century, turning Canada into a net FDI capital exporter by 1997 for the first time since the country's founding, reversed course. Dominated by large foreign acquisitions of Canadian natural resource companies beginning in 2006, Canada recorded

1 The most immediate cycle began in the fourth quarter of 2001 when it rose from its 2002-based index of 97.8 to 122.5 in the fourth quarter of 2007, representing a 25.3% increase in six years.

a net FDI inflow of $27.0 and $62.3 billion in 2006 and 2007, respectively. This positive capital inflow undoubtedly reinforced and bolstered the term-of-trade-inspired rise in the Canadian dollar over the past two years. All told, the Canadian dollar has surged 78.5% in value relative to the U.S. dollar in just six years — a surge that is without precedent since the Government of Canada freed the Canadian dollar to float on the market in 1971 (see Figure 2).[2]

The Bank of Canada is further forecasting Canadian real GDP growth rates of 1.4% and 2.4% in 2008 and 2009, respectively. This forecast, made in April 2008, is predicated on U.S. real GDP growth rates of 1.0% and 1.7% in 2008 and 2009. Although these U.S. GDP annual growth rates are positive, the Bank of Canada does recognize that there is a good chance the recently slumping U.S. residential housing market, declining U.S. consumer confidence, and the large twin deficits of the U.S. federal government budget and the U.S. current account may conspire to drive the U.S. economy into recession in the first quarter or even the first half of 2008. These projections, therefore, point to an economic turnaround in the latter half or three-quarters of 2008, but they will nevertheless act as a further drag (over and above the high value of the Canadian dollar) on Canadian exports to the United States over the next two years.

The above predictions are, in general, shared by a number of forecasting outfits, but one would be remiss if one did not also recognize a diversity of opinions exists. For example, although acknowledging the possibility of a looming U.S. economic recession, the Conference Board of Canada is slightly more optimistic in forecasting U.S. real GDP growth rates of 1.6% and 2.5% in 2008 and 2009, thus leading to continued higher growth of Canadian real GDP of 2.2% and 3.0% in 2008 and 2009, respectively.

Labour Market Performance

With Canadian real GDP growing rapidly and steadily as it has in the past several years, not surprisingly Canada's labour market has also performed well in this period. Aggregate employment in Canada has grown from 15.6 million in January 2003 to 17.0 million in December 2007, thereby improving 1.4 million or 9% in just five years (see Figure 3). Job creation has been spectacular, averaging more than 280,000 per annum in this period. The employment rate has also increased steadily to 63.9% by March 2008, while the overall unemployment rate in Canada has hovered just below 6.0% for the past six months, even declining to 5.8% before returning to 6.0% in March 2008 — both of these statistics have respectively established a 33-year high/low in the process.

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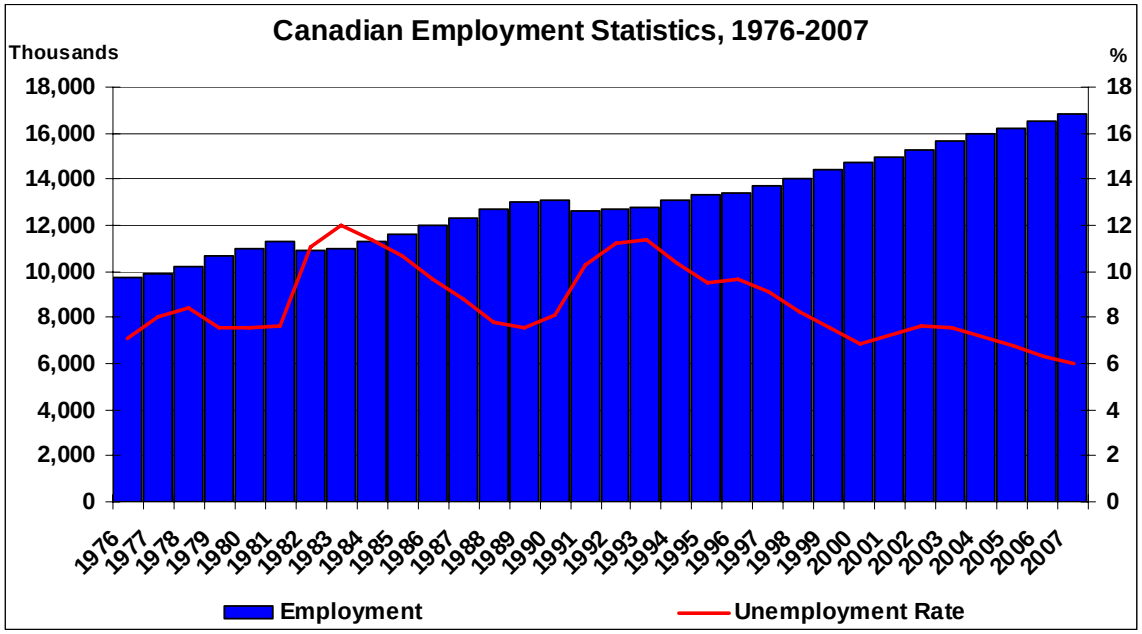
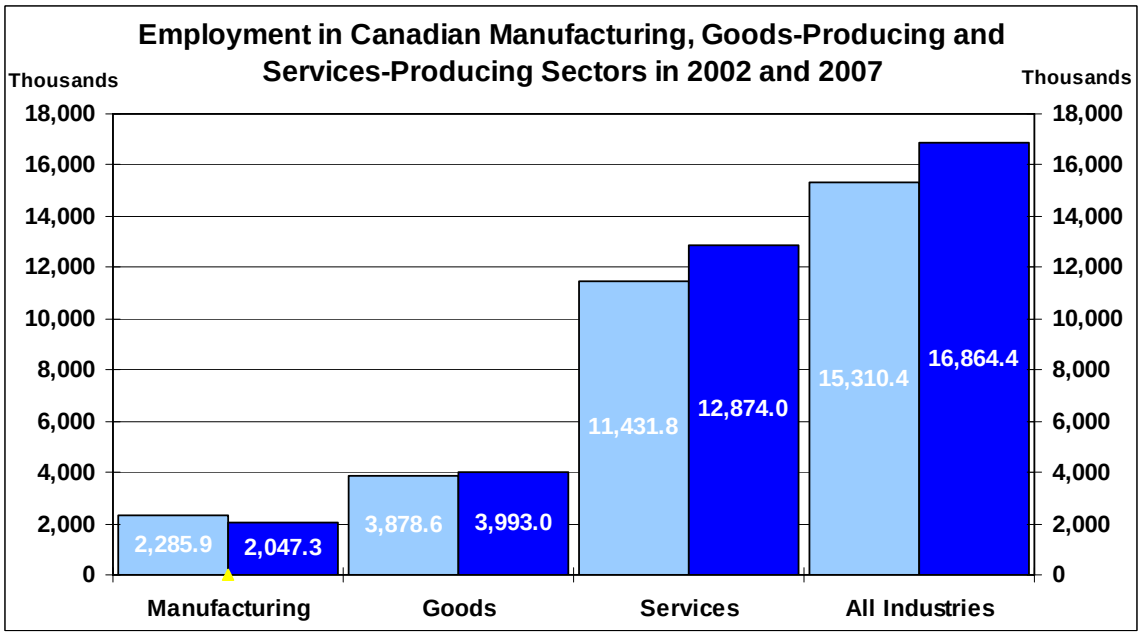
2 The comparison is made between the base case (denominator) of 61.79¢ US on January 21, 2002 and its peak of US$1.1030 on November 7, 2007.

Figure 3



Source: Statistics Canada, Labour Force Survey, various dates.

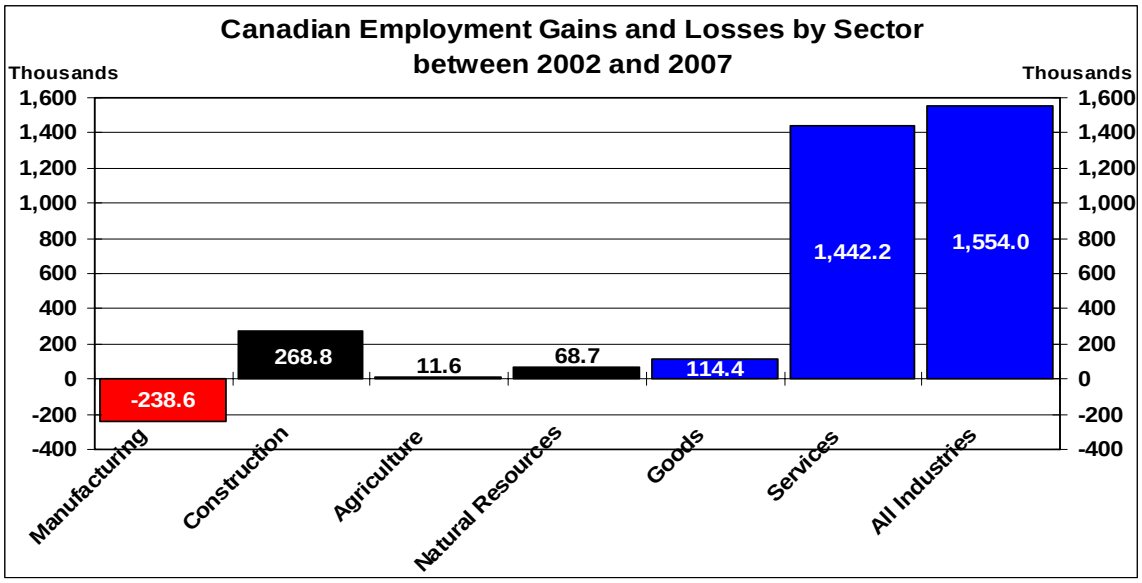
Figure 4



Source: Statistics Canada, Labour Force Survey, various dates.

This employment growth has been widely felt throughout the economy, except in the manufacturing sector (see Figures 4 and 5). Services sector employment grew from 11.4 million in 2002 to 12.9 million in 2007 or by 14.1%. The goods-producing sector includes the manufacturing sector, as well as agriculture, natural resources, utilities and construction sectors. Employment in the manufacturing sector declined from its peak of 2.3 million in November 2002 to 2.0 million in March 2008, resulting in the loss of approximately 352,900 workers or 15.1% of its employed labour force in November 2002. However, agriculture, natural resources, utilities and construction sectors more than made up for the loss in employment in the manufacturing sector, as the goods-producing sector grew its employment from about 3.9 million in 2002 to about 4.0 million in 2007 or by 2.3%.

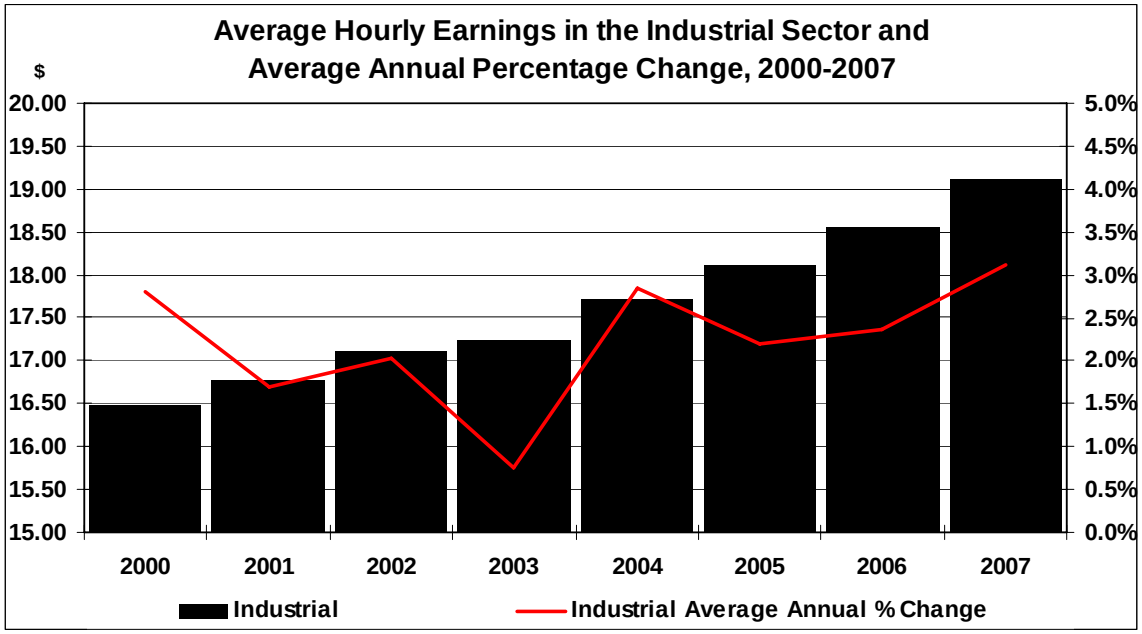
Figure 5



Source: Statistics Canada, Labour Force Survey, various dates.

The relatively tight Canadian labour market (in historical terms) has also resulted in rapidly rising wages and benefits. The average industrial wage has risen from $16.49 to $19.13 between 2000 and 2007, representing an average annual increase of 2.1% (see Figure 6). Indeed, Canadian hourly wages have risen much faster since the “commodities boom” began; they have increased, on average, by 2.6% per annum in the past four years. Given that price inflation has averaged 2% in this period, Canadian workers have made significant real income gains since 2003.

Figure 6



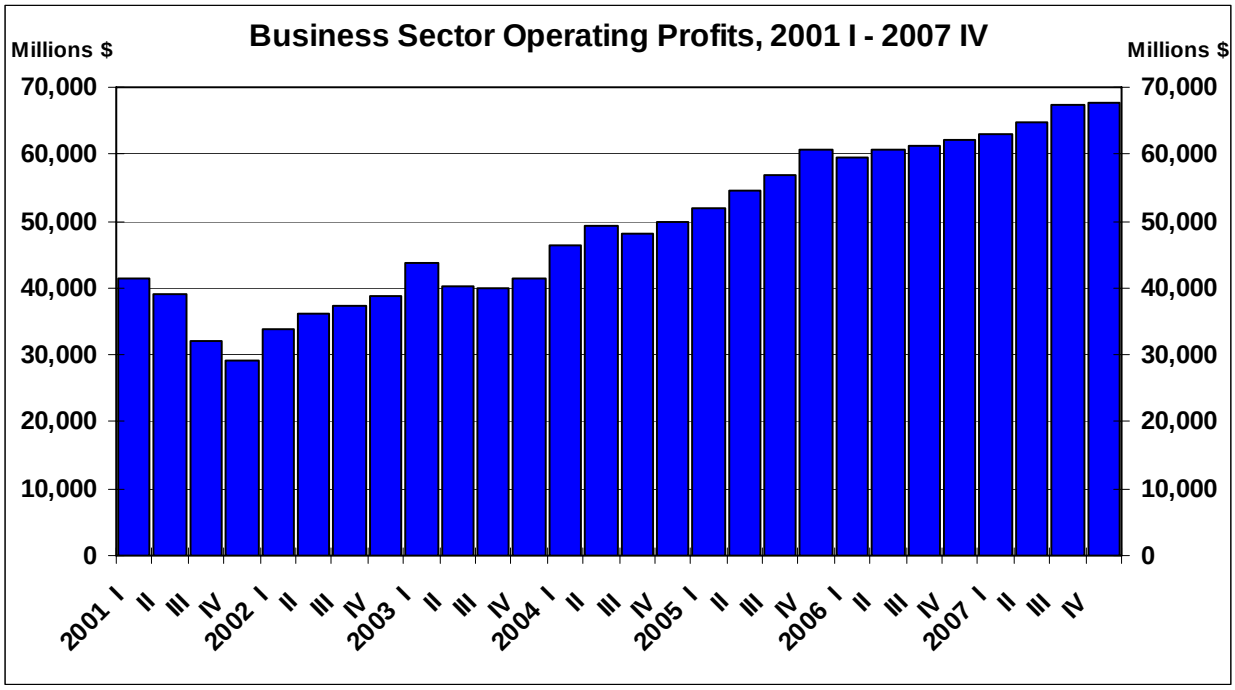
Source: Statistics Canada, CANSIM Table 282-0087.

Business Sector Performance

Business sector profitability has improved markedly over the 2000-2007 period. Operating profits in the business sector of $173.1 billion in 2000 declined for just one year before rebounding and growing in each successive year until reaching $262.5 billion in 2007, representing an increase of almost 52% in the past seven years (see Figure 7). Indeed, Canada's business sector has repeatedly reported a new all-time high operating profit performance in each successive year since 2004. Almost in lock step, profit margins, return on equity, and return on capital employed in the business sector have also tracked higher in this period; they reached 8.8%, 12.1% and 8.7%, respectively, in 2007.

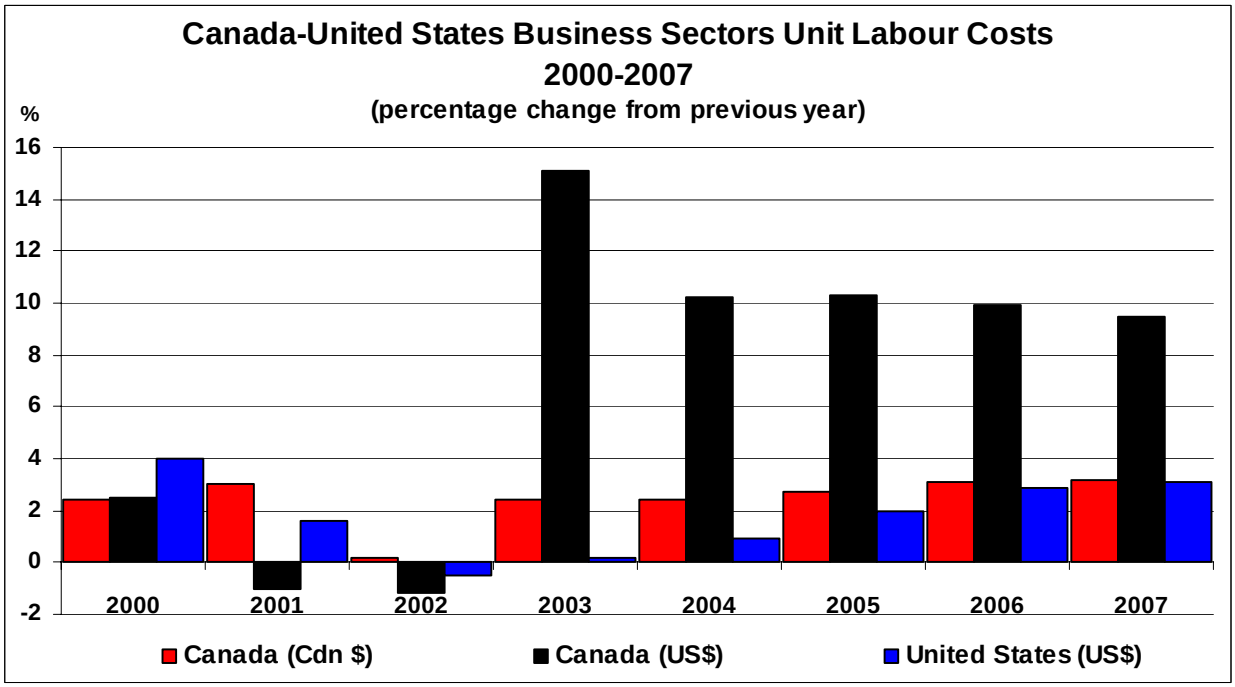
Unfortunately, Canada's business sector has not performed well relative to the U.S. business sector in terms of productivity or competitiveness. Labour compensation per hour in the business sector has risen significantly more rapidly than labour productivity in Canada since 2000 — approximately 21% versus 7%, respectively — and, therefore, unit labour costs in Canada have risen by about 14% between 2000 and 2006 (see Figure 8). More importantly, after accounting for an appreciating Canadian dollar against the U.S. dollar, the Canadian business sector's unit labour costs in U.S. dollar terms have risen by more than 50% between 2000 and 2006. The U.S. business sector, by comparison, has experienced only a 7% rise in its unit labour costs.

Figure 7



Source: Statistics Canada, Quarterly Financial Statistics for Enterprises, various dates.

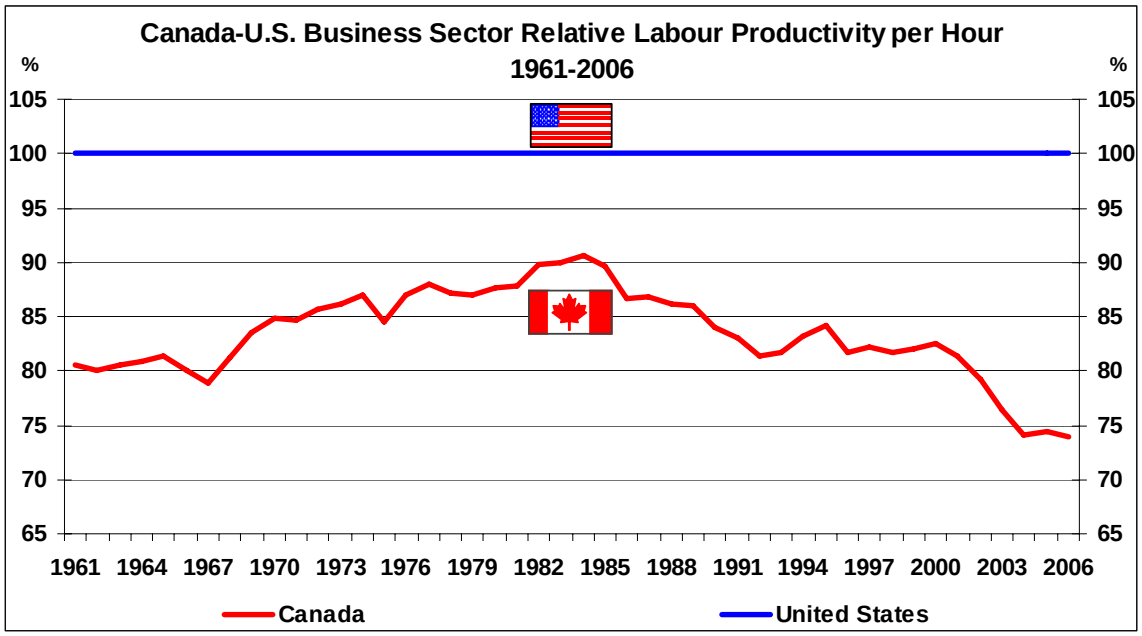
Figure 8



Source: Statistics Canada, The Daily: Labour productivity, hourly compensation and unit labour cost, various dates.

In trying to isolate a cause for Canada's relatively poor cost competitiveness with the United States, one immediately observes that hourly compensation has been quite comparable between the two countries, but hourly compensation in the United States has risen only slightly more than labour productivity in the United States. Thus, one difference in the performances between the business sectors of the two countries has been that of labour productivity, which in the United States rose by 17.5% compared to 6.4% in Canada between 2000 and 2006. However, Canada's poor competitiveness against the United States since 2003 is, first and foremost, the result of a large and rapid appreciation of the Canadian dollar against the U.S. dollar. It can explain almost three-quarters of the 43 percentage point difference in unit labour costs. One caveat though: the rise in the Canadian dollar against the U.S. dollar is a business condition that is beyond the control of the business sector; only the business sector's labour productivity performance is a business condition under the direct control of the sector.

Figure 9



Source: Centre for the Study of Living Standards, http://www.csls.ca/data/iptjune2007.pdf, Table 7a.

Canada's poor labour productivity performance relative to the United States is not a recent development; it is a continuing saga that began in the mid-1980s (see Figure 9). In 1984, Canadian business sector's labour productivity relative to that of the United States reached its modern-day peak of 90.6%, but it has steadily declined to 74.0% in 2006.

CHAPTER 2
THE SERVICES SECTOR

There have been two dominant economic forces driving structural change of the Canadian economy away from manufacturing and towards services, one long term and, apparently, perennial, the other more recent and indeterminate in duration. For more than five decades, the demand for services by Canadians has been growing rapidly, both in absolute terms and relative to that of goods. This force and its effect on the industrial structure of the economy have largely gone undetected by the public, as the growth in demand for services has been subtle but persistent. More recently, the worldwide "commodities boom", described in some detail above, is directly and indirectly forcing a restructuring of the economy towards the natural resources and services sectors and away from the manufacturing sector. Although the positive impact on the natural resources sector from a "commodities boom" is rather obvious, the positive impact on the services sector is not immediately apparent. The demand for services by Canadians has been indirectly buoyed by the "commodities boom" according to the following chain of events: (1) the greater receipts earned by Canada's natural resources sector, followed by large investments — sometimes a takeover — in Canadian companies, has led the Canadian dollar to appreciate in value (to balance the payments between Canada and the rest of the world); (2) an appreciation of the Canadian dollar has, in turn, made imported goods more competitive and has forced a slowdown in overall retail price increases across Canada; (3) retail price increases, which have been lower than personal income increases for the better part of five years, have *defacto* augmented both the purchasing power and the wealth of Canadians; and (4) Canadians, buoyed by greater real personal incomes, have continued to purchase disproportionately more services than goods. Like the longer-term trend towards more services, this latter force and its effect on the structure of the economy, which is entering its sixth consecutive year, has also gone undetected by the public, largely because it has been overshadowed by layoff and shutdown announcements in the manufacturing sector. Each of these trends will, in turn, be described in more detail in the following sections.

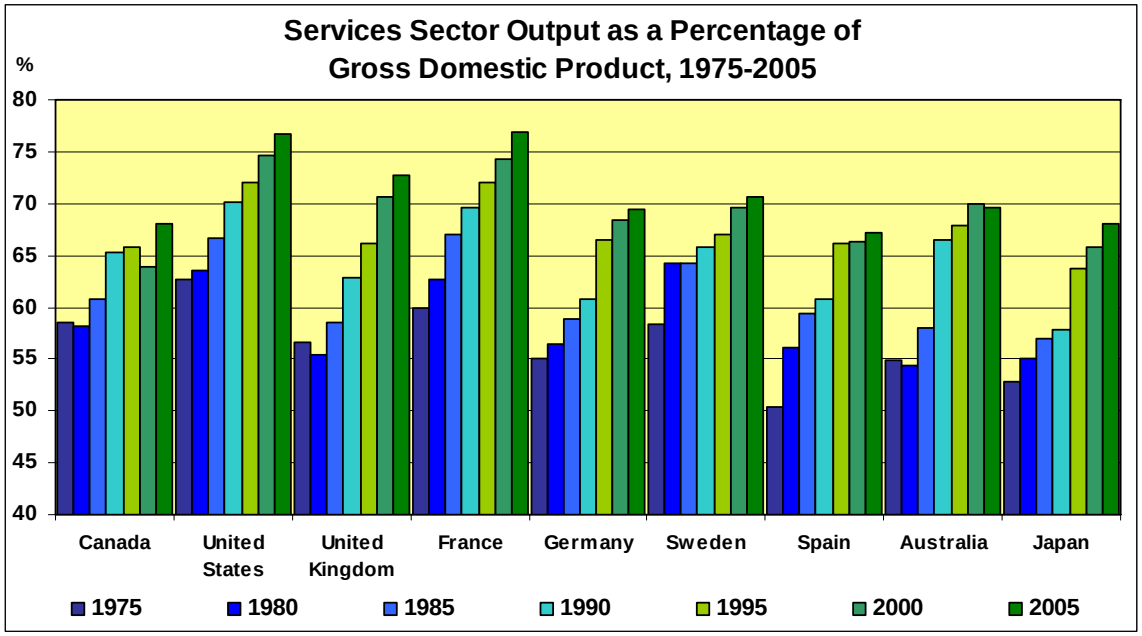
Economic Contribution and Structural Change

Services consist of diverse activities that together, in 2007, accounted for almost 70% of GDP and more than 75% of employment in Canada. By way of comparison, the services sector contributes more than four and six times what the manufacturing sector contributes to GDP and employment, respectively, which amounted to 15.1% of GDP and 12.1% of employment in 2007.

This large contribution made by the services sector to the Canadian economy was not always so. Services have been growing far more rapidly and consistently than the goods-producing sector throughout the past five decades. Thus, the shares of services in total economic activity and employment have been increasing steadily over time. For

example, in 1975, services output accounted 58% of Canada's GDP, and this share had grown to 68% by 2005 (see Figure 10). This development suggests that Canada's economy has been undergoing profound, long-term structural change away from goods-producing activities and towards services — at least in percentage terms.[3]

Figure 10



Source: World Bank, World Development Indicators, 2007.

Canadians' growing appetite or demand for services (in both absolute and relative terms) is not unique. Indeed, the long-term trend away from goods-producing and towards services-producing activities is found in many developed economies throughout the world. For example, as Canada's services sector grew from 58% to 68% of GDP between 1975 and 2005, France led the way, growing its services sector from 60% to 77% of GDP. France was followed (in order of share of GDP in 2005) by the United States, the United Kingdom, Sweden, Australia, Germany and Japan. In 2005, all of these countries had a

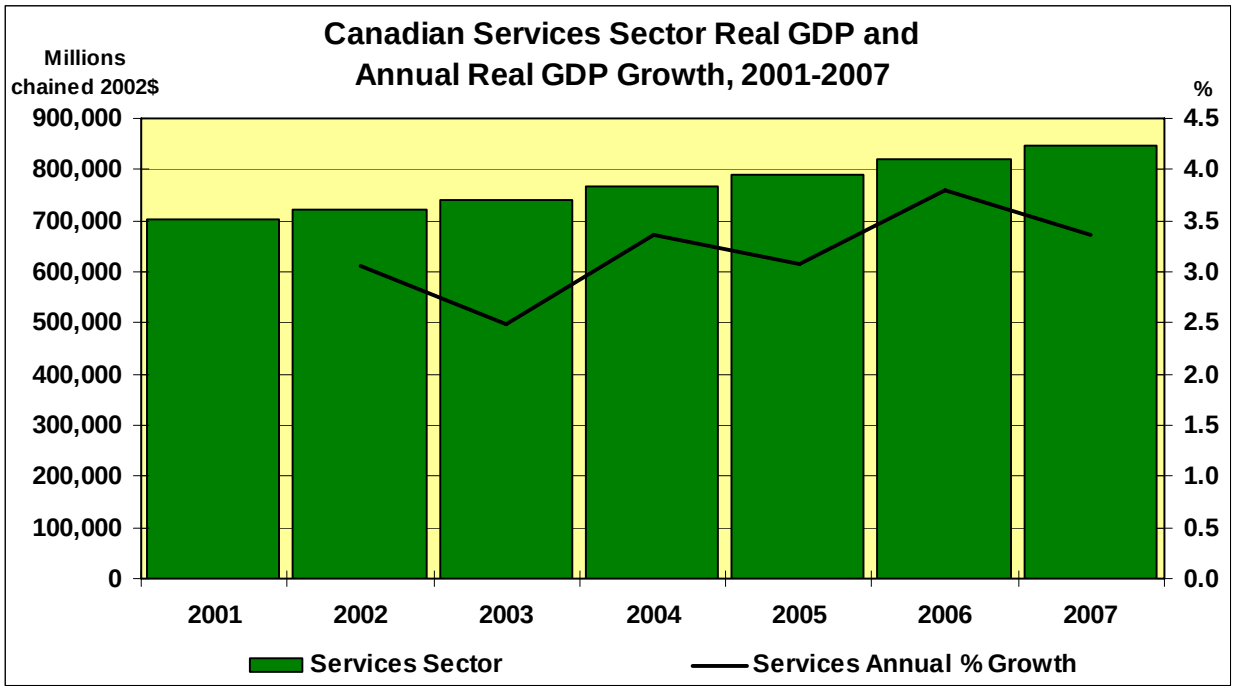
3 An important caveat is in order. The implied growth rate of the services sector using its percentage contribution to GDP over the past 30 years is, in part, a statistical artefact. With the large shift of the "baby boom" generation to two-income families from its predecessor generation that was predominantly composed of one-income families, whereby one parent withdrew from the paid labour force and engaged in domestic chores — that is, house cleaning, snow shovelling, lawn care, child care, child tutoring, meal preparation, etc. — which are not included in the calculation of GDP, these activities were increasingly contracted out to independent companies whose activities are included in the GDP calculation. Furthermore, previously illegal and strictly controlled activities, such as gambling, that mostly did not enter the GDP calculation are increasingly captured in the GDP calculation today. All of these activities are largely services and, thus, past services sector contributions to GDP were vastly understated statistically. Although the services sector's contribution to GDP remains understated statistically — though less so today — the growth rate of the services sector's contribution to GDP is likewise overstated.

services sector that accounted for a greater share of GDP than did Canada. Of the eight comparator countries found in Figure 10, only Spain trailed Canada in terms of its services sector share of GDP.

Economic Performance

Against this long-term economic backdrop favouring services over goods, the current business cycle, spearheaded by a worldwide "commodities boom," is indirectly reinforcing structural change in favour of services in Canada. Indeed, services sector real GDP has grown from $701.1 billion to $846.4 billion between 2001 and 2007, or approximately by 20.7% in the past six years (see Figure 11). Average annual growth of services sector GDP has therefore been 3.4%, which is about half a percentage point greater than the average annual growth rate of the Canadian economy in this period.

Figure 11

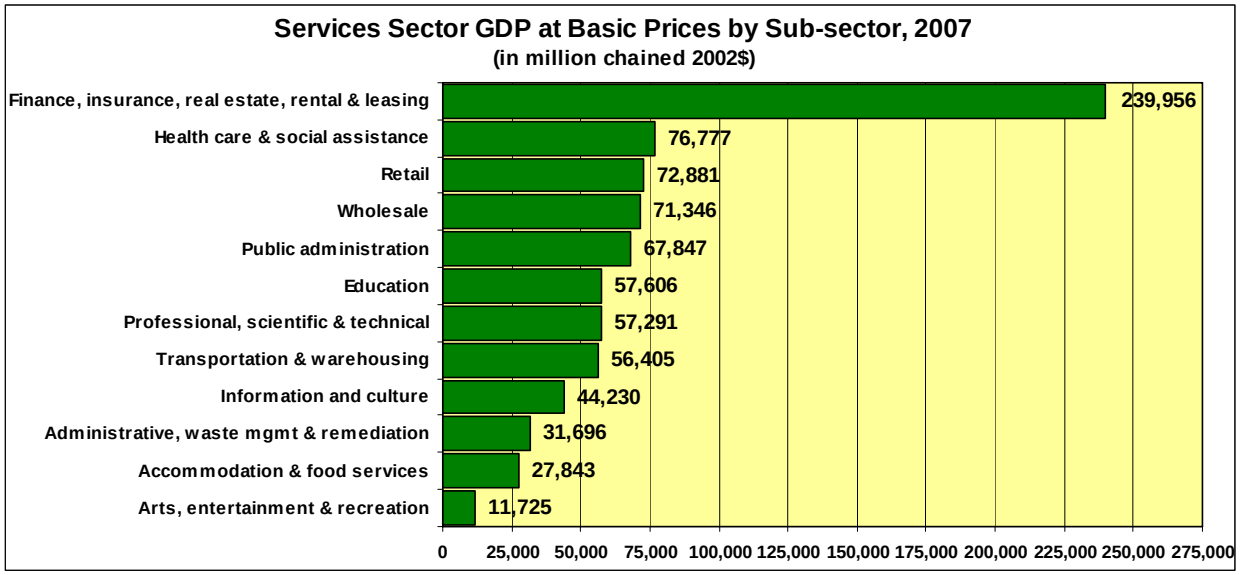


Source: Statistics Canada, *Canadian Economic Observer*, various dates.

As mentioned above, the services sector incorporates many diverse activities, some of which are included in the business sector and some of which are not; Statistics Canada includes the latter services under the non-business sector. For example, industries with large proportion of public funding, such as health care and social assistance, public administration and education, are included in the non-business sector, and they make major contributions to GDP. Indeed, health care and social assistance, public administration and education have been growing relatively rapidly over the past several

decades and, today, account for almost one-quarter of services sector GDP. Individually, these three public services sub-sectors are respectively the second, sixth and seventh largest services sub-sectors in Canada (see Figure 12).

Figure 12



Source: Statistics Canada, CANSIM Table 379-0017.

Growth of services within the business sector component has been fastest within wholesale trade, retail trade, and administrative support and waste management. Growth has been slowest in arts, entertainment and recreation, and accommodation and food services. In 2007, the five largest industries of the business services sector were: (1) real estate, rental, and leasing; (2) finance and insurance; (3) retail trade; (4) wholesale trade; and (5) professional, scientific and technical services.

Services Co-operatives

As somewhat alluded to above, services provision can be organized under a for-profit corporation, the principal organizational type used in the business sector, or under a not-for-profit corporation, the principal organizational type used in the non-business sector (using Statistics Canada's terminology, meant to combine the public or volunteer sectors of the economy). An interesting but often overlooked organizational type is the co-operative organization. Some co-operatives provide services rather than goods and, in the process, they often straddle both business and non-business sectors. In Canada, co-operatives can be found providing financial services through credit unions and *caisses populaires*, insurance, retail goods, health care, childcare and agricultural services.

More formally, a co-operative is a legal entity owned and democratically controlled equally by its members. Co-operatives are often organized as non-capital stock corporations under state-specific co-operative laws. They may, however, be organized as business corporations or unincorporated associations. Each co-operative has, as part of its mandate, the commitment to help its community (and also many co-operatives sustain the wider world community through their contributions to co-operative international development programs). Co-operatives do not generally pay dividends, but return savings or profits, sometimes known as patronage, to their members.

In 2007, there were more than 9,000 co-operatives in Canada that employed over 170,000 people and had assets totalling more than $260 billion. In addition, almost 100,000 individuals volunteer their time in helping manage the co-operatives by sitting on boards and committees. Co-operatives have some 18 million individual memberships, representing at least 13 million Canadians. This means that four in ten Canadians are members of a co-operative. The federated co-operatives have returned some $450 million in patronage dividends to local member retail co-operatives. In addition, credit unions gave back some $34.7 million in 2006 in the form of donations and contributions to community economic development; the Co-operators Group allocated $3.5 million in 2006 into community projects; and Mountain Equipment Co-op put 1% of its sales, or $2.4 million, into climate change projects in Canada.

In today's globalized world, in which for-profit corporations are pursuing greater profits and maximizing shareholder value — sometimes leading to the flight of banks and retail stores from many inner cities and rural and remote communities — co-operatives have been increasingly noted for remaining in these communities, filling important gaps in services provision to its members.

Export Performance

Although services make up the greater share of domestic commercial activity and goods make up a much smaller share, the situation is entirely reversed when it comes to the international trade data. In 2007, Canada exported $67.5 billion and imported $86.9 billion in services, yielding a services trade deficit of $19.5 billion. Given that total Canadian exports and imports were $532.7 billion and $502.5 billion in 2007, respectively, services accounted for only 13% of exports and 17% of imports. Commercial services make up the bulk of Canadian services trade, and trade balances do not favour Canada in the most significant components of services trade.

It would be premature, however, to conclude that Canadian services make an insignificant contribution to Canada's international trade account. With globalization marked by the forging of global supply chains, whereby corporations integrate trade, both imports and exports, within their worldwide production plant networks in a way that allows them to optimize the functioning of their global operations, trade in services is largely embedded in the trade of goods and capital investments. In effect, many services are not traded directly,

but indirectly when they are integrated or embedded in the goods that are traded. For example, an American built or assembled airplane may rely on a component designed, produced and marketed in Canada. In this supply chain, Canada's statistical agency records the export of the aerospace product, which is then aggregated in Canada's merchandise goods account, yet the engineering and design services, as well as other managerial services, may make up the most significant cost component in this traded aerospace product. Moreover, continuing with this example, had the Canadian engineers provided only the blueprints of the aerospace product to the American airplane producer for it to manufacture in the United States, then Canada's statistical agency would record the trade under Canada's services account. Comparing these two alternative trading arrangements, the latter would record a much smaller amount of Canada-U.S. trade than the former, but the transaction would also be entirely recorded as a trade in services, whereas the former would be recorded as a trade in goods. The latter trading arrangement, thus, accurately records the amount of Canadian services exported, whereas the former understates the amount of Canadian services exported. Yet clearly more Canadian services are produced and ultimately exported to the United States under the former trading arrangement.

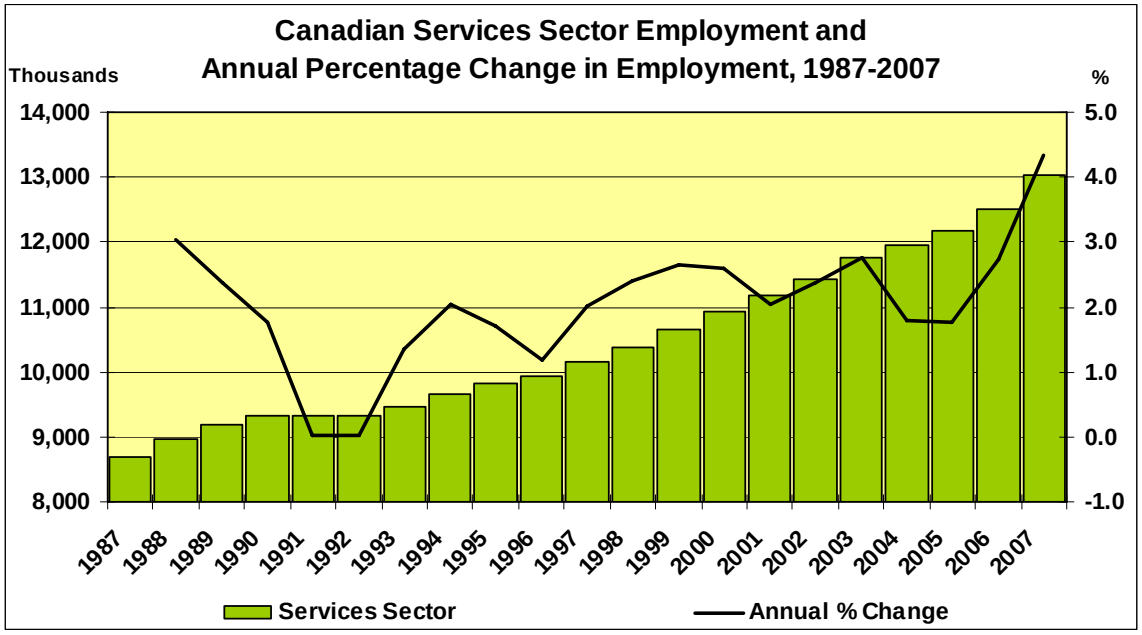
Globalization has seen enormous growth in traded goods and services. Although Canada exported only $67 billion in services in 2006, Export Development Canada estimates that Canadian companies with foreign operations sell about $140 billion worth of services each year.

Employment Performance

Employment in Canada's services sector has also enjoyed long-term robust growth. Services sector employment approached 12.9 million in 2007, growing each year, on average, by 2% since 1987 (see Figure 13). This performance has picked up markedly since the "commodities boom" began, as the services sector grew on average by 2.4% per annum between 2002 and 2007. Indeed, the services sector accounted for almost 93% of the increase in employment in Canada between 2002 and 2007.

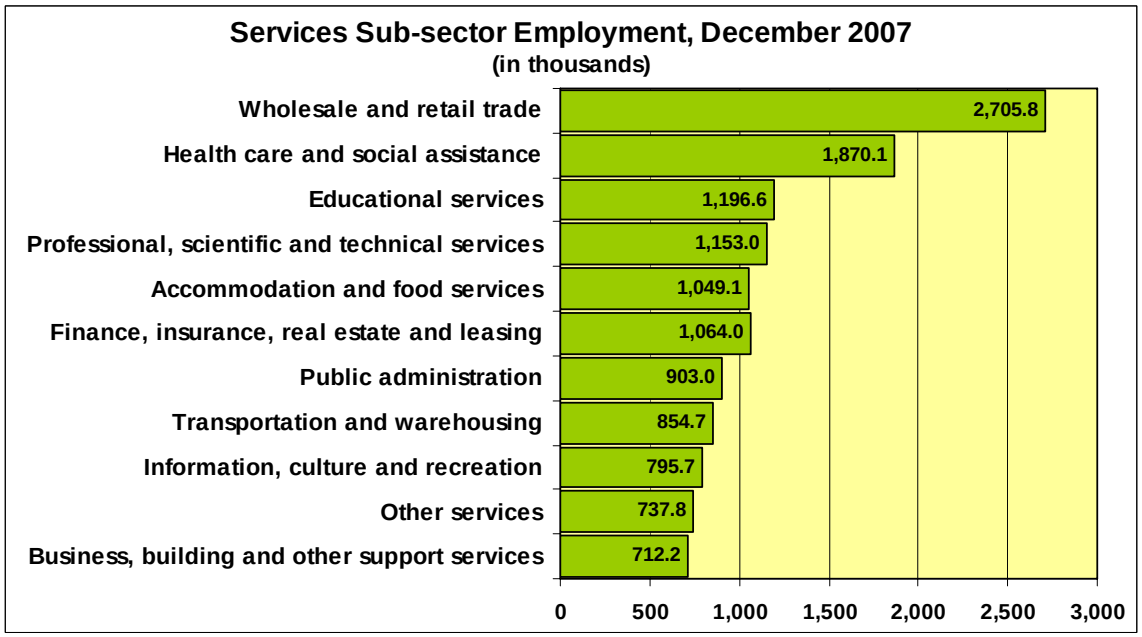
In the past five years, the largest increases in services sector employment have occurred in retail trade, health care and social assistance, and administrative support and waste management. In term of total employment in 2007, the top five services sub-sectors are: (1) retail trade; (2) health care and social assistance; (3) education; (4) accommodation and food services; and (5) public administration. One will observe that the order of these industries does not reflect the same order of the top five services sub-sectors in terms of contribution to GDP (compare Figures 12 and 14). Differential labour-intensities across the sector largely explain the re-ordered industry rankings.

Figure 13



Source: Statistics Canada, CANSIM Table 281-0024.

Figure 14

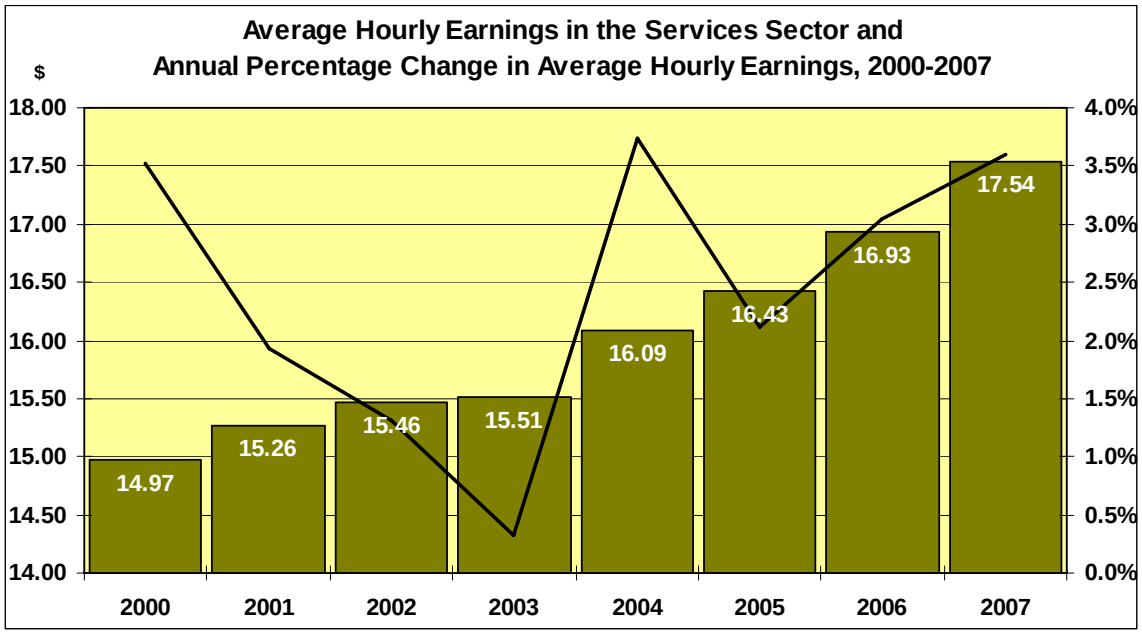


Source: Statistics Canada, Labour Force Survey, January 2008.

Wages and Earnings

Canada's relatively tight labour market has resulted in rising wages and benefits in the services sector. The average services sector wage has risen from $14.97 to $17.54 between 2000 and 2007, representing an average annual increase of 2.4% (see Figure 15). Hourly wages have also risen much faster since the "commodities boom" began; they have increased, on average, by 3.1% per annum in the past four years. Given that price inflation has averaged 2% and other sectors of the economy have experienced lower average wage increases in this period, Canadian services sector workers have made significant real and relative income gains since 2000.

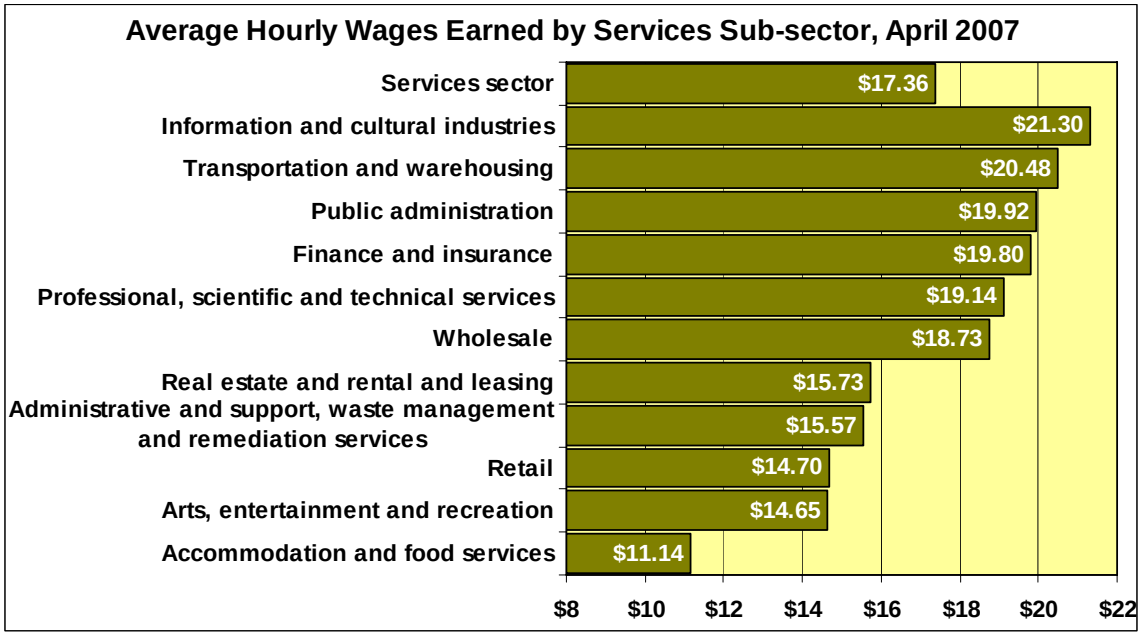
Figure 15



Source: Statistics Canada, CANSIM Table 282-0087.

The diversity of activities comprising the services sector is also reflected in the wages paid by the various services sub-sectors. Wages range from an average of $11.14 per hour in the accommodation and food services industries, though this does not take into account the gratuities received by employees in these industries, to an average of $21.30 per hour in the information and cultural industries (see Figure 16). Sub-sectors paying wages greater than the average services sector wage include information and cultural industries, transportation and warehousing, public administration, finance and insurance, and professional, scientific and technical industries. Sub-sectors paying wages less than the average services sector wage include real estate and rental and leasing industries, administrative and support, retail trade, arts, entertainment and recreation, and accommodation and food services industries.

Figure 16



Source: Statistics Canada, CANSIM Table 282-0087.

Innovation

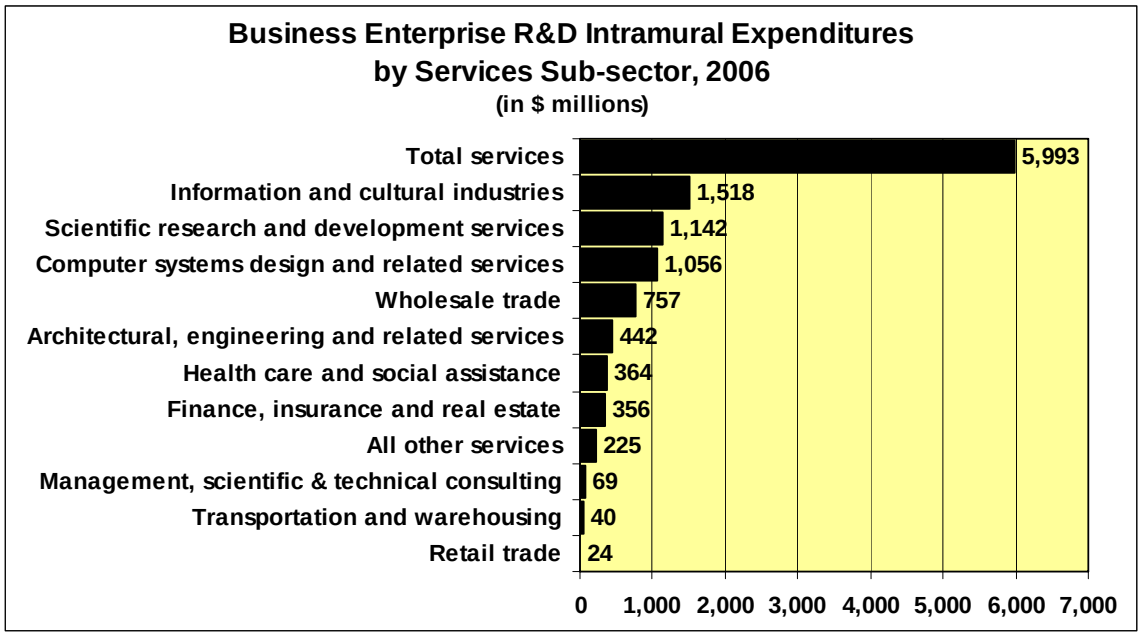
Innovation often underlies the ability of Canada's services sector to grow and compete internationally. Whether it is new processes resulting from intensive research and development (R&D), enhanced training or education, data storage, improved regulations or deregulation, or a new design and marketing strategy, innovations make the sector a better place to work, more efficient in providing services to Canadians, and more competitive.

Examples of innovation in the services sector include the move toward more internet banking; remote surgery; electronic health records; radio frequency identification (RFID) in retail stores, passports, the NEXUS system at the Canada-U.S. border, and for road tolls such as the 407 in the Toronto area. These and other innovations in the services sector are supported and, indeed, made possible by R&D across the sciences, social sciences and humanities. To be at the cutting edge of developing and implementing services sector innovations, Canada has had to invest in "blue sky", basic and applied research, as well as import the results of foreign R&D.

Innovation can confer a competitive advantage on the providers of services, particularly those that are tradable internationally, but if this advantage is to endure, an intellectual property (IP) regime — that is, copyright, trademark and patents — that appropriately balances creator and user rights is essential. Accordingly, IP issues deeply concern and affect a broad range of service activities, such as technological breakthroughs

in information and communications technology (ICT) services (e.g., the Blackberry); the distribution of television, Internet, books and other cultural products; and piracy and counterfeiting in the retail industry.

Figure 17



Source: Statistics Canada, CANSIM Table 358-0024.

Canadian businesses within the services sector spent almost $6 billion on R&D in 2006 (see Figure 17). This intramural R&D spending included $1.5 billion by the information and cultural industries, $1 billion in computer system design, and $1.1 billion in scientific, research and development services. In addition, the information, communications technologies industry spent $5.7 billion on R&D in manufacturing and services.

CHAPTER 3
INDUSTRY CHALLENGES AND RESPONSES

FINANCIAL SERVICES INDUSTRY

1. Economic Contribution

The financial services industry is made up of a variety of entities, including banks, trust and loan companies, credit unions and *caisses populaires*, life insurance companies, property and casualty insurance companies, securities dealers, and leasing advisers. The industry is one of a small number of key pillars of the economy, playing a critical role in the allocation of capital and the distribution of risk across the economy.

The financial services industry has been growing in terms of its contribution to GDP: in the 1980s, the industry accounted for about 4.5% of GDP; in 2006, it accounted for 6.2% of GDP. The industry also employed about 700,000 Canadians, representing about 4% of national employment. In addition, finance and insurance companies contributed more than 44% of Canada's direct investment abroad in 2006.

2. Industrial Structure

The provision of financial services is dominated by the banking industry, which includes 73 banks: 21 domestic banks (Schedule 1), 24 foreign banks (Schedule 2), 22 foreign full service branches and six foreign lending branches (Schedule 3). The industry is heavily concentrated, as the "big six banks" — RBC Capital Markets, TD Securities, CIBC, BM Capital Markets, Scotia Capital Inc. and Banque Nationale — account for about three-quarters of the assets in the deposit-taking sub-sector in Canada, which is valued at about $1.8 trillion. The provincial entities, such as the *caisses populaires* and the credit unions, account for about 12% of assets and the foreign banks for about 9%.

In 2007, there were about 100 life insurance companies in Canada. These companies employ about 51,000 people, but the industry accounts for about 120,000 people when including advisers, assessors and adjusters. This industry is also very concentrated. The "big three life insurers" — Manulife, Sun Life and Great-West Life — account for about 60% of domestic net premiums, followed by 53 foreign life insurers, accounting for 22% of premiums, and other domestic smaller companies, accounting for 18% of premiums.

In 2007, there were about 214 property and casualty insurance companies employing about 110,000 Canadians, 40% of which were directly working for the property and casualty insurers and 60% of which were brokers and adjusters. This industry is not concentrated. The largest entity, ING, accounts for about 11% of net premiums. Foreign companies in Canada account for about 58% of the net premiums earned.

3. Challenges

The banking industry believes that they are facing increased competition due to key actions taken by governments elsewhere:

- United Kingdom's financial services authority has moved from detailed/prescriptive rules to principles-based regulation to provide greater flexibility while ensuring strong oversight;

- U.S. Treasury has launched a regulatory streamlining initiative, explicitly aimed at enhancing competitiveness;

- New York City has undertaken a major study on how it can improve its competitiveness and reverse recent losses of market share to London;

- Australia reorganized and simplified its regulatory structure, moving from state-level regulation to one national prudential regulator and one consumer regulator.

Regulations (e.g., a common securities regulator) and capital and corporate taxes are important challenges that governments need to address to ensure the continued competitiveness of the industry.

In addition, the financial services industry, like other industries, is concerned about the impending skills shortages as suggested by simple arithmetic:

retiring baby boomers + declining fertility rates = shrinking labour force.

The life insurance industry also identified two public policy deficiencies: (1) insufficient data on the services sector; and (2) the lack of meaningful commitments to liberalize services trade in the WTO's DOHA round of negotiations.

Property and casualty insurers were concerned about aging inner city and municipality infrastructure, like sewage and water systems.

4. Industry Responses

Since 1990 the federal government has been reviewing the banking industry's impaired-loans-to-total-loans ratio. At first blush, it appears that the banks are getting better at executing their intermediation function, though the apparent good results could be a function of the strong economy. Both banks and insurers have very strong capital positions vis-à-vis the requirements that the Office of the Superintendent of Financial Institutions (OSFI) requires of them.

REAL ESTATE, RENTAL AND LEASING INDUSTRY

1. Economic Contribution

The real estate, rental and leasing industry contributed $148 billion to Canadian GDP and employed 245,725 Canadians in 2006. The real estate, rental and leasing industry is the largest contributor by far to Canadian GDP in the services sector; it contributes almost two times what the second largest industry, healthcare and social services, contributes. Since it is not a labour-intensive industry, however, it is a relatively small employer within the services sector.

2. Industrial Structure

Real estate agents assist Canadians in buying and selling real estate, representing buyers, sellers or both in these transactions. They make property evaluations and subsequently advise on appropriate asking and offer prices. The industry is regulated by provincial real estate councils in six of 10 provinces (Alberta, British Columbia, Nova Scotia, Ontario, Quebec and Saskatchewan). In 2005, there were 98,813 people licensed to buy and sell real estate in Canada. Alberta, British Columbia, Manitoba, New Brunswick, Nova Scotia, Ontario and Saskatchewan have signed a mutual recognition agreement whereby agents moving from one province to another or working in more than one province are evaluated only on their knowledge specific to the province in which they wish to work.

The Canadian Real Estate Association (CREA) represents real estate brokers, agents, and salespeople working through more than 100 real estate boards and associations in all provinces and two territories in Canada. CREA owns the MLS trademark as well as the REALTOR trademark. The REALTOR trademark provides an assurance of integrity and can only be used in Canada by members of CREA who accept and respect a strict code of professional conduct. The code requires members to subscribe to free and open competition according to the principles embodied in the *Competition Act* of Canada.

The real estate database systems, operated under the MLS trademark, provide an inventory of available properties and ensure maximum exposure on the Internet of properties listed for sale across Canada and throughout the world. In 2007, MLS/SIA sales totalled $118.3 billion, an increase of 19.6% over the previous record set in 2006.

3. Challenges

CREA expects residential sales to decline somewhat in 2008, but it believes that the Canadian situation is nowhere near as bad as it appears in the United States. The housing crisis in the United States resulted from poor lending standards. Risky loans were made to homebuyers with poor credit, on the assumption that rising prices would make up for any lending mistakes. When buyers began defaulting on these loans and lenders subsequently foreclosed on their mortgages, houses began to flood the market and lenders ended up losing large amounts of money. By contrast, Canada's housing market is built on strong employment growth and consumer confidence, not easy access to cheap credit. In Canada, only 5% of all mortgages are classified as sub-prime, whereas approximately 20% is so classified in the United States. However, while CREA believes that house ownership activity has been strong, it also believes that rental housing activity has been extremely weak.

The Competition Bureau recently completed a study of the regulated professions (including real estate agents) and did not find any major restrictions in the real estate industry.[4] The Competition Bureau found that barriers to entering the real estate profession are quite low; the supply of real estate agents is large (compared with the supply of other professionals) and that the market was highly competitive. The Competition Bureau did, however, raise a particular concern in the case of Ontario. The Competition Bureau found that Ontario regulations limit price competition in that "there is no opportunity to choose from a menu of services, or to pay a flat rate for some services and a commission on the sale price, to maintain an incentive for the agent to seek the highest possible price". The Competition Bureau recommended the removal of this restriction.

4. Industry Responses

CREA's response to the poor rental housing market has been to propose to the federal government to defer the capital gains tax and the recapture of the capital cost allowance when an investment property is sold and the proceeds of the sale are reinvested in another property within one year. CREA believes that such a measure would reduce the cost of rental housing and make it more affordable, as well as increase the housing stock.

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4 Competition Bureau, Self-regulated Professions: Balancing Competition and Regulation, 2007, at http://www.competitionbureau.gc.ca/epic/site/cb-bc.nsf/vwapj/Professions%20study%20final%20E.pdf/$FILE/Professions%20study%20final%20E.pdf.

PROFESSIONAL SERVICES INDUSTRY

1. Economic Contribution

Canada combines professional, scientific and technical services into one classification within the services sector. This classification includes legal, accounting, tax preparation, bookkeeping, architectural, engineering, specialized design, computer systems design, management, science, technical consulting, advertising and other professional services. In 2006, Statistics Canada reported employment of 704,909 professional services providers. Architectural, engineering and related service providers accounted for 155,923 employees or 22% of those employed in the professional, scientific and technical services sub-sector; followed by computer system designers at 139,444 or 20%; accounting, tax preparation and bookkeeping at 86,168 or 12%; 83,662 management, scientific and technical consulting or 12%; and 66,874 lawyers and other legal service providers or 10%. These five broad groupings thus represent more than three-quarters of those employed in the professional, scientific and technical services sub-sector.

Professionals are playing an increasing role in Canadian society and its economy. Today's increasingly integrated and fast-paced world is demanding more advanced, innovative and competitive services from professionals. In fact, some claim that these services are the foundation on which the knowledge-based economy is being built, and that Canada's professionals are integral to the success of Canadian businesses, goods and services sectors alike. As such, Canada's professionals are punching above their weight, particularly in terms of their economic contribution which amounted to $57.3 billion in 2007, representing 4.7% of Canadian GDP. In return, these professionals were paid, on average, $19.14 per hour in 2007, which is 10.3% higher than the average of $17.30 paid to those working in the larger services sector.

2. Industrial Structure

Some of these professionals are certified, licensed and regulated; notable examples include lawyers and accountants. The economic rationale for regulation of the professions — both direct (provincial or territorial) government regulation and rules of self-regulation imposed by professional organizations on their members — is to protect consumers and guard the public interest. Both governments and the professions themselves recognize that consumers do not (in a number of circumstances) possess the requisite information to accurately assess the quality of services they need or have received. Certification and entry restrictions into the professions, along with other regulations or rules governing conduct, by and large attempt to correct for the potential for sub-standard service to be delivered in these circumstances. Some regulations, however, may inadvertently stray beyond this public interest purpose — acting as a barrier to entry

and may make collusion among providers more likely — and thus adversely affect competition in terms of price, service price-quality trade-offs, and the breadth of product/service selection.

Three associations of these professions appeared before the Committee: accountants, management consultants and engineers. Beginning with the accountants, although there are generally no legal restrictions on who may practise accounting in Canada, some jurisdictions regulate public accounting. Furthermore, all accountants in Canada are subject to the rules and regulations of their respective designations which, in Canada, there are only three recognized by provincial and territorial statute: Chartered Accountant (CA), Certified General Accountant (CGA) and Certified Management Accountant (CMA). Individuals seeking to become accountants in Canada must have a university degree, pass the required professional education courses and accumulate a certain amount of work experience.

The Canadian Institute of Chartered Accountants, along with the provincial and territorial CA organizations, represent approximately 72,000 CAs in Canada and Bermuda. National, provincial and territorial CGA organizations represent approximately 68,000 CGAs in Canada, Bermuda, the Caribbean, Hong Kong and China. CMA-Canada represents 38,000 CMAs in Canada and around the world. According to Statistics Canada, 154,200 or 81% of 191,200 accountants in Canada are employed by a firm, whereas 36,200 or 19% of all accountants are self-employed.

Somewhat in contrast to accountants, management consultants are not regulated. In part because it is not regulated, according to CMC-Canada, the Canadian management consulting industry is best characterized as “an atomistic market”, whereby there are many players in the marketplace and no one firm is large enough, relative to the market as a whole, to have any appreciable effect on price. Hence, there are no artificially constructed barriers to entry by regulation (however unintended).

Currently, there are 2,400 CMCs practising in Canada and a further 800 members of CMC-Canada who have yet to gain their designation, representing about 13% of an estimated 25,000 management consultants in Canada. In 2006, management consulting industry in Canada generated gross revenues of approximately $9.3 billion.

3. Challenges

The various associations representing the professions advanced a number of similar challenges, as well as others which appear to be best characterized as being on “opposite sides of the coin” in terms of the advantages and disadvantages conferred by regulation.

Beginning with the similar challenges, a number of the professions suggested prior consultations between the federal government and the professional representative bodies are required — as they affect their respective rights and obligations — before further negotiations of the WTO General Agreement on Trade in Services (GATS) take place. In a related vein, Canadian management consultants often confront non-tariff barriers while competing for management consulting contracts in some countries, usually in the developing world. Furthermore, despite Canadian management consultants being granted reciprocal temporary entry privileges to the United States under appendix 1603-D-1 of the NAFTA, they are often stopped or detained at the border for what CMC-Canada characterizes as frivolous reasons when working on projects in the United States for Canadian clients.

In terms of challenges that appear to be on “opposite sides of the regulatory coin”, CMC-Canada complains that there is currently no effective way to prevent anyone, including “charlatans (i.e., superficial celebrities and dubious experts) from hanging out a shingle, calling themselves management consultants and offering their services”. CMC-Canada and the provincial institutes devote significant effort to warning potential clients of the dangers of hiring such individuals and to encourage them to hire only those who can demonstrate their qualifications of background, education and experience through their membership in CMC-Canada. Unfortunately, this is only a partial solution, and clients will still have unfortunate experiences with no recourse if the consultant is not a certified management consultant.

Professional bodies of accountants and lawyers control such problems more effectively through regulation; that is, through imposing entry and other restrictions on their members and their conduct. However, unlike CMCs who enjoy reciprocity of services provision not only across the country but in over 25 countries around the world, these same restrictions often inadvertently suppress competition and mobility throughout the country. In fact, the Competition Bureau completed a recent study of the regulated professions (including medical professions) that found numerous instances of regulation that may restrict competition more than necessary. Hence, achieving the appropriate balance between regulation and competition would appear to be at the heart of this challenge.

4. Industry Responses

CMC-Canada has spent significant time trying to make it easier for its members to do their business in other countries by expediting members’ entry into the United States for temporary business purposes, by reconciling the definition of management consultant under GATS and NAFTA with industry practice, and by trying to level the playing field for foreign contracts.

HEALTHCARE INDUSTRY

1. Economic Contribution

In 2007, Canadians spent $160 billion on healthcare. Healthcare contributed $76.8 billion or 6.3% to Canadian GDP. In 2007, more than 1 million people were employed in the healthcare field. Women filled 80% of jobs in the healthcare industry.

2. Industrial Structure

The healthcare field is best characterized as a continuum of services from acute care, home and community care, public health, mental health and family services. These services are delivered in a variety of ways from large teaching hospitals to individual practitioners. Primary health care is generally funded by provincial governments, with some services covered by insurance and private funds. Fields such as dental care or chiropractic services are predominantly private sector funded. For example, $10.8 of the $11.3 billion spent on dental care in 2007 was private sector spending.

3. Challenges

Inaccessibility to services was cited as the main challenge in healthcare services. In the publicly funded healthcare field, inaccessibility and long wait times are caused by too few health care professionals or lack of equipment. In private care such as dentistry, problems with access are generally caused by high fees, with some Canadians unable to pay for the high cost of treatment and therefore going without care.

Canada's aging population will place additional demands on the healthcare system as seniors typically have greater healthcare needs than younger people. At the same time, the health workforce is also aging: approximately 38% of the nursing workforce is more than 50 years old and nearing retirement, and the average age of the health workforce was 41.9 in 2005, 2.3 years older than the general Canadian workforce. In addition, younger professionals are, in general, choosing to work fewer hours than their older colleagues, and parents of young children, particularly women, often prefer shorter work weeks. All of this suggests that, in the absence of additional equipment, significant technological innovation and/or different (possibly streamlined) treatment practices, more than one recruit will be needed to replace each upcoming retiree to provide the same level of healthcare, let alone what might be required to meet the increasing demand that demographic trends imply.

With the industry's unemployment rate of only 1.2% in 2006 and employers struggling to fill vacant positions, recruitment and retention of healthcare professionals are already major challenges in healthcare. Unless action is taken to address it, the shortage of personnel in healthcare appears likely to get worse.

Chiropractors find it difficult to become involved in mainstream care. Even when they are granted privileges in hospitals, patients often have to pay privately for that care.

4. Industry Response

Some provinces are taking innovative approaches to recruitment by providing bursaries to students in return for signing a return to service agreement. Nunavut offers a nursing program through Nunavut Arctic College, and part of the Nunavut Nurse Recruitment and Retention Strategy involves graduating more Inuit nurses. The Late Career Initiative in Ontario encourages nurses over age 55 to stay in the profession by offering them teaching and mentoring positions, rather than front line duties.

Some dentists are addressing the problem of people not being able to afford care by offering pro-bono services on an informal basis.

RETAIL TRADE INDUSTRY

1. Economic Contribution

Retail sales totalled $412 billion in 2007, growing by 5.8% in the past year. Retail trade output or value-added was estimated at $72.9 billion in 2007, accounting for 6% of GDP. The retail trade employed more than 1.7 million Canadians in 2007, which represented 10% of Canada's employed labour force. In all but three provinces (Prince Edward Island, Manitoba and Saskatchewan), the retail trade is the largest employer industry.

2. Industrial Structure

There were more than 227,000 retail stores in Canada in 2004, 41,498 of these were chain stores (i.e., defined as four or more locations under one owner). Franchises are another major segment, but they are difficult to quantify.[5] Broadly speaking, there are about six retail outlets per 1,000 persons in Canada.

Food and beverages (22.1%), motor vehicles (22.0%), furniture, home furnishings and electronics (9.1%), health and personal care products (8.4%), and clothing, footwear and accessories (8.4%) are the largest retail industries by sales. Together, these five commodity groupings accounted for 70% of retail sales in 2004. Canada's 80 largest retailers accounted for more than 35% of non-automotive retail sales.

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5 Paul Jacobsen, The Structure of Retail in Canada, http://www.ic.gc.ca/epic/site/retra-comde.nsf/en/h_qn00134e.html, 7 January 2007.

3. Challenges

The rising Canadian dollar has highlighted many price discrepancies between Canadian and U.S. retail sectors, and many Canadians located close to the Canada-U.S. border are choosing to shop in the United States rather than in Canada, simply because of these price differences. Same-day automobile trips to the United States by Canadians were 23.4 million in 2006, while same-day automobile trips to Canada by Americans were 13.7 million. Canadian cross-border shopping in the United States is clearly on the rise, as Canadian same-day automobile trips to the United States have increased by 2.6 million from 20.8 million recorded in 2002, when the Canadian dollar began its ascent.

In general, Canadian retailers incur higher labour costs than U.S. retailers. Also contributing to higher retail prices of similar goods in Canada compared to in the United States are import duties and different Canada-U.S. labelling requirements (i.e., English versus bilingual, Imperial versus metric weights and measures) when sourcing products from the United States.

The retail sector is experiencing labour shortages, particularly acute in Alberta. Annual labour turnover rates across Canada are averaging 30%, whereas they are 60% to 70% in some regions of Alberta.

4. Industry Responses

The retail industry has increased pay rates from 76% of the average industrial wage in 1999 to 88% in 2006. The industry invests in considerable in-house training, building company specific skills but also many transferable skills.

The retail industry is working with universities and colleges to develop certification programs for careers in retail sales. They are also working with Aboriginal communities to prepare people for careers in retail.

FOOD SERVICES INDUSTRY

1. Economic Contribution

The food services industry recorded sales of $53 billion in 2006, representing 3.8% of GDP. Over one million people are directly employed in the food services industry, accounting for 6.3% of total Canadian employment, and another 240,000 jobs indirectly depend on the food services industry as suppliers, distributors and consultants. It is further estimated that the food services industry also supports 20% of Canadian agricultural jobs. Between 2007 and 2010, foodservice sales are expected to grow by 0.5% after inflation.

2. Industrial Structure

There are 63,000 food services establishments in Canada. About two-thirds of them are locally owned and operated. The industry reports the average tenure of an employee within the industry has increased from 37.6 to 45.4 weeks between 1987 and 2007.

3. Challenges

The food services industry is very competitive and operates on small profit margins. For example, the pre-tax profit margin for the average food services operator in 2005 was 3.8%, compared with 8.8% for the average Canadian business.

The decrease in the number of international tourists has adversely affected the food services industry, as have increasing energy, labour and food costs. As a result, there are 1,180 fewer food services operators in 2007 than in 2001.

The food services industry faces labour shortages. Many food service positions are entry level jobs and 45% of employees are under 24 years of age. As the number of youth in Canada decreases in the coming years, the industry expects increasing challenges in filling positions. This labour challenge is especially acute in Alberta where some restaurants have had to turn customers away even though they have empty tables because they do not have enough staff to serve them.

4. Industry Responses

In Alberta, the Canadian Restaurant and Foodservices Association is working with other agencies involved in tourism to advocate expanding tourism studies in high schools and post secondary institutions.

TRAVEL AND TOURISM INDUSTRY

1. Economic Contribution

Tourism is a $66.9 billion industry in Canada, accounting for 2.3% of GDP. There are 633,000 full time jobs in the tourism sector, and another one million jobs depend on tourism in some way. In 2006, tourism generated $19.4 billion in tax revenues, including $9.1 billion at the federal level.

2. Industrial Structure

There are over 200,000 tourism businesses in Canada, 80% of which are small and medium-sized enterprises. These businesses include accommodations, attractions, tour operators, travel agents and visitor reception centres.

3. Challenges

Canada has seen a decrease in international tourists in recent years. About 28.9 million international tourists came to Canada in 2006, down from 40.9 million in 2003. Americans, who make up around 90% of visitors to Canada, account for most of this decline in tourists. Canada's tourism trade deficit has grown from $1.7 billion in 2002 to $7.2 billion in 2006, and is expected to be more than $8 billion in 2007.

There are a number of reasons for the decline in U.S. tourists. The rising of the value of the Canadian dollar against the U.S. dollar is an important factor, but high fuel prices, lengthy wait times at the border, confusion surrounding passport requirements, and a relative shift towards more exotic holiday destinations have all contributed.

Canada spends less than other countries, such as Australia, marketing to similar audiences. In addition, provincial advertising may be confusing to prospective international tourists, who might not immediately associate Nova Scotia or Alberta, for example, with a holiday in Canada.

4. Industry Responses

The tourism industry is working with the Canadian Tourism Human Resources Council to create awareness of opportunities for skilled professionals in the tourism sector.

The 2010 Winter Olympics and Paralympics in Vancouver and Whistler offer an opportunity to promote Canada to the world, and the industry is working to take advantage of this opportunity.

The Tourism Industry Association has re-branded Canada as "Canada — Keep Exploring".

TRANSPORTATION INDUSTRY

1. Economic Contribution

Commercial transportation industries contributed $45.8 billion or 4.3% to Canadian GDP in 2006.[6] Trucking made the greatest contribution, accounting for $15.1 billion or 1.4% of GDP, followed by rail at $6.0 billion or 0.6% of GDP, air at $4.7 billion or 0.4% of GDP, and urban transport at $3.2 billion or 0.3% of GDP. Other transportation industries include interurban and rural bus, scenic and sightseeing, postal and courier services, as well as support activities for other modes of transportation, such as baggage handling, pilotage, harbour operation and rail car loading and unloading.

2. Industrial Structure

A. Trucking Industry

For-hire carriers, private carriers, owner-operators and courier firms make up the trucking industry. This industry generated an estimated $67 billion in revenues in 2005.

In 2005, there were more than 10,000 for-hire motor carriers in Canada that earned $30.4 billion in revenues. The 100 largest for-hire trucking operations in the United States and Canada in 2005 (ranked by revenue) included six Canadian carriers: TransForce Income Fund (22nd), Montreal, Quebec; Trimac Transportation Services (43rd), Calgary, Alberta; Day and Ross Transportation group (50th), Hartland, New Brunswick; Vitran Corp (60th), Toronto, Ontario; Contrans Income Fund (73rd), Woodstock, Ontario; and Mullen Group Income Fund (95th), Aldersyde, Alberta.

In 2005, there were an estimated 36,000 owner-operators who primarily hauled their own freight. Couriers and parcel-delivery firms operated 2,000 trucks, providing some of the same services as for-hire carriers. In 2005, the courier industry generated an estimated $6.4 billion in revenue.

B. Rail Industry

The rail industry generated revenues of $9.8 billion in 2005, with the Class I carriers — CN, CPR and VIA Rail — accounting for about 93% of this revenue. Shortline rail revenues were $455 million in 2005, accounting for 5% of rail industry revenues.

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6 Industry GDP contributions are expressed in constant 1997 dollars.

VIA Rail remains the dominant intercity passenger rail company, accounting for almost 94% of total passenger revenues in 2005. Intercity rail passenger services are also provided by CN (former Algoma Central Railway services), Ontario Northland and the Quebec North Shore and Labrador. Seasonal and tourist operations in Canada include The Great Canadian Railtour Company, Alberta Prairie Railway Excursion, White Pass and Yukon, the Hull–Chelsea–Wakefield Railway and Prairie Dog Central. Amtrak, an American corporation, offers service to Montreal, Vancouver and Toronto (the latter in conjunction with VIA Rail).

C. Airline Industry

Air passenger traffic was a record 68.2 million in 2006. Air Canada provided approximately 61% of the Canadian air carrier industry's overall domestic scheduled capacity, with Jazz providing approximately 96% of Air Canada's regional air services capacity. WestJet provided approximately 29% of the Canadian air carrier industry's overall domestic scheduled capacity.

Many air carriers provided charter air services for inclusive package tour operators between Canada and Europe, the United States, the Caribbean and other leisure travel destinations, including Air Canada, Westjet, Canjet, Air Transat, Skyservice, Harmony Airways, Zoom Airlines and Sunwing Airlines. A number of air carriers provided cargo air services for Canada Post, courier companies, freight forwarders, consolidators and shippers, including Cargojet Canada (Mississauga), Kelowna Flightcraft (B.C.) and Morningstar Air Express (Edmonton). The volume of goods carried by Canadian air carriers was 689.3 million metric tonnes in 2005.

3. Challenges

The airline and trucking industries share similar challenges when it comes to high and rapidly rising petroleum prices, including the federal excise tax of 4¢ per litre on jet fuel and diesel, but they also face industry-specific challenges.

Both transportation industries are fuel intensive, with the trucking industry reportedly consuming more than 16 billion litres annually. Although motor carriers have been able to pass some of this increase on to their customers through fuel surcharges in the past, current economic conditions within the industry make this increasingly difficult to accomplish. For this reason, both industries complain that the federal excise tax on motor fuels, which was introduced in the 1980s as a deficit-fighting measure, has outlived its stated purpose.

The airline companies also complain of the current airport rent regime. Every year the Government of Canada collects between $200 million and $300 million in rents from not-for-profit airport authorities. In addition to rent, the air traveller security charge

represents another critical element of taxation policy deserving of reconsideration. The airline industry claims that, according to the Department of Finance, air transport security charge now has a surplus of more than $80 million and that, since its inception in 2002, it has taken $200 million in excess revenues.

The high value of the Canadian dollar and the general weakening of the U.S. economy have resulted in a reduction of Canadian exports to the United States which, in turn, are having a profound adverse impact on the trucking industry in most parts of the country.

4. Industry Responses

Both trucking and airline industries responded to these uncontrollable events through mergers and consolidation. With high fixed costs, low margins and crude oil hovering at around US$100 a barrel, the larger airline companies have been vigilant in ensuring their sustainability through reinventing themselves in response to the new permanent reality of a low-cost air travel business model.

INFORMATION AND COMMUNICATIONS TECHNOLOGIES INDUSTRY

1. Economic Contribution

The information and communications technologies (ICT) industry includes telecommunications, cable and satellite television, computer hardware and software, and the Internet. The ICT industry is comprised of 32,000 companies: software and computer services (79%), ICT wholesaling (11%) and ICT manufacturing (7%). The industry contributed $65 billion to Canadian GDP in 2006, accounting for 5.9% of GDP.

There are about 600,000 jobs in ICT companies, about three quarters of them in services, and there are also about 500,000 ICT workers in other sectors of the economy.

In 2006, the ICT industry spent $5.7 billion on R&D, and accounted for 39% of total Canadian industrial research and development expenditure.[7] ICT companies top the list of Canadian industrial spending on R&D: Nortel Networks 2006 spent $2.2 billion and was followed by Bell Canada Enterprises with $1.4 billion (Magna international was third at $650,000).[8] Most ICT research is performed by the manufacturing sub-sector but, in 2006, $2.5 billion was spent on R&D by software and communications services.

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7 Industry Canada, Canadian ICT Sector Profile, http://strategis.gc.ca/epic/site/ict-tic.nsf/en/h_it07229e.html.

8 From Research Infosource Inc., Canada's Top Corporate R&D Performers 2007, http://www.researchinfosource.com/2007-top100.pdf.

2. Industrial Structure

Over 97% of ICT companies are small in size. According to Industry Canada, 81% of companies employ one to nine personnel, 14.3% employ 10 to 49 personnel, and 2.6% of companies have 50 to 100 employees. Medium to large size companies account for only 2.4% of the sector. There are approximately 120 large companies with over 500 employees.

Between 16-20% of ICT workers are self employed. In 2006, about 10% of the ICT industry workforce was composed of internationally educated professionals and non-permanent residents.

3. Challenges

The ICT sector is facing an acute skills shortage. In 2008, there are expected to be 25,000 vacant ICT jobs in Canada, and only 8,000 new graduates to fill them. This shortage is expected to grow to 100,000 skilled workers by 2009 and to 1 million by 2016.[9] Moreover, despite the low unemployment rates and high wages in the ICT sector, university enrolment in relevant degrees decreased by 11% between 2002 and 2005. The problems can be seen as early as secondary school, with too few people pursuing mathematics and computer sciences.

Canada lacks a strong anti-counterfeiting regime. Piracy rates of Microsoft products in Canada are 33%, which compares with 21% in the United States.

4. Industry Responses

To address the shortage of skilled personnel in Canada, the industry is developing a number of initiatives:

- On-shoring, bringing talent to Canada, rather than off-shoring work internationally, particularly to India. For example, Microsoft is hiring internationally, primarily from India and China, to fill vacancies at is new software development site in British Columbia. Canada's immigration procedures, and quality of life, currently give it an advantage in this regard.

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9 Branham Group Inc, Current snapshot of the Canadian ICT Labour Market, Information and Communications Technology Council, Ottawa, March 2007, p. 3, available at http://www.ictc-ctic.ca/uploadedFiles/Labour_Market_Intelligence/Snapshot%20Current%20State.pdf.

- A strong emphasis on internal training (e.g., IBM invests about $350 million per year on internal training).

- Microsoft has launched “School of the Future”, including one in the York region of Toronto, which aims to give students the skills they will need for the careers of the future.

- IBM has launched “EXCITE”, a program focused on getting 12-13 year-old girls interested in science and engineering.

- Microsoft has a program called “Partners in Learning” to train teachers of grades 6 to 12.

- Co-op programs at universities, particularly the University of Waterloo.

CULTURAL INDUSTRY

1. Economic Contribution

The cultural services industry includes activities such as broadcasting, performing arts, design, bookselling, magazines, newspapers, sound recordings, printed music, visual arts, festivals and sporting events. In 2002, the cultural industry contributed about $39 billion to GDP, or 3.9% of GDP, and employed 597,700 people.[10] Written media was by far the biggest contributor to culture GDP in 2002, accounting for 47% of culture GDP, followed by broadcasting (13%) and the film industry (9%). In term of employment, written media was again the largest sub-sector (158,900), followed by the film industry (88,700), broadcasting (55,200), advertising (48,600), design (43,700), heritage (35,900), libraries (24,600), and the performing arts (23,700).

In 2004, Canada recorded a $500 million trade deficit in cultural services, with imports of $3.5 billion and exports of $3.0 billion.

10 Statistics Canada, *The Impact of the Culture Sector on the Canadian Economy*, http://dsp-psd.pwgsc.gc.ca/Collection-R/Statcan/87-004-XIE/0010387-004-XIE.pdf.

2. Industrial Structure

In 2002, 21% of cultural workers were self employed, and there are many small firms. For example, the bookselling industry is comprised mainly of small businesses, with over 70% of booksellers having less than 1 million dollars of annual sales. Many of these smaller companies are struggling, and 365 small booksellers have closed in Canada since 1996.

3. Challenges

Many cultural sectors pay relatively low wages, and because they are often self-employed, cultural sector workers may not have access to Employment Insurance. In addition, many cultural sector workers, such as actors, do not have a steady income and would benefit from a special tax provision that would allow them to average their incomes over an extended period.

Since 1999 there has been a drop in Canadian television productions, making it hard for Canadian actors to find work. Industry participants expressed concern over the potential of foreign ownership of Canadian broadcasting companies.

The high value of the Canadian dollar is adversely affecting the number of Hollywood productions being filmed in Canada.

Industry participants claim that non-licensed booksellers such as Amazon.com are able to sell books at cheaper prices, in part, because they are not subject to the same rules as booksellers that are physically located in Canada.

4. Industry Responses

Booksellers are working to have publishers lower their prices, since it is they, not the booksellers, who determine the book cover price.

GAMING INDUSTRY

1. Economic Contribution

Legalized gaming is the largest segment of the entertainment industry, with revenues of $14.6 billion in 2006. Gaming revenue is comparable in size to revenues for movie rentals, television, music and professional sports combined. The gaming industry

contributes $8.6 billion to government and charities. Gaming is responsible for 135,000 full-time jobs, and another 130,000 depend on gaming in some way.

2. Industrial Structure

The gaming industry encompasses a broad range of activities including lotteries, casinos, racetracks, electronic gaming devices (also known as video lottery terminals (VLTs)), and online gaming activities. There are 65 casinos, 38 racinos and racetracks, and over 250 bingo halls across Canada. Recent growth in the industry has been attributed to the expansion of casino facilities and electronic gaming devices.

3. Challenges

The gaming industry faces social concerns associated with acute or chronic problem gambling. Between 0.5% and 1.5% of gamblers have a gambling problem. Canadian provinces spent $90 million annually on problem gambling treatment.

4. Industry Response

The gaming industry acknowledges its responsibility to provide safe and secure venues to assist individuals who are playing beyond their limits, but states that this is not straightforward undertaking as external organizations cannot remove an individual's right to make decisions.

CHAPTER 4
POLICY INSTRUMENTS AND OPTIONS

Services Sector Policies

The Government of Canada has not developed a services sector-specific industrial policy, but through various programs supports both the goods sector and the services sector in Canada. One overarching services sector issue raised by many witnesses was the general unavailability of data, at least insufficient data for the needs of the sector's analysts. Effective data collection and dissemination are essential for government, individuals and enterprises in the public and private sector to make evidence-based decisions. Although data is collected and analyzed across a range of service industries, more data on the services sector as a whole is needed to enhance understanding and allow for greater analysis of the sector. The Committee, therefore, recommends:

> **That the Government of Canada continue to improve Statistics Canada's collection and dissemination of data on the services sector.**

The Committee also found that often overlooked in the services sector is the contributions made by the co-operative movement. Canada's economy includes more than 9,000 cooperatives, with more than 170,000 employees and total assets of over $260 billion. Indeed, 13 million Canadians, or 40% of the population, are members of a co-operative.

Canada's co-operatives are found in many services sub-sectors such as financial services, retail, housing, daycare, recreational facilities, electricity and water supply. Despite this diversity of business activities, the federal government provides oversight of co-operatives through its Co-operatives Secretariat, which has been organized within Agriculture Canada since it was established in 1987. The Committee questioned the placement of the Secretariat within Agriculture Canada, given the strong engagement of the movement in the services sector. Indeed, representatives of co-operatives were the first to question this organizational structure, as they believe that it does not accurately reflect the diversified nature of the co-operative movement. They suggested moving the Co-operatives Secretariat to Industry Canada. The Committee agrees. Although the Committee recognizes the historical dominance of agricultural cooperatives within the co-operatives movement in Canada, it believes that the Secretariat's placement within Agriculture Canada does not reflect the diversified character of co-operatives in Canada. The Committee, therefore, recommends:

> **That the Government of Canada move the responsibility for the Co-operatives Secretariat from Agriculture Canada to Industry Canada.**

Labour Policy

Over the past decade, three main factors have shaped Canada's workforce: (1) an increasing demand for skills in the face of advanced technologies and the high pace of growth of the "knowledge based economy"; (2) a working-age population that is increasingly made up of older people; and (3) a growing reliance on immigration as a source of skilled labour. Added to this mix of long-term trends is a recent structural development that is forcing a reallocation of labour, both from one sector of the economy to another (i.e., from the manufacturing sector to other goods-producing sectors and the services sector), and from one region of the country to another (from eastern and central Canada to western Canada).

Table 1
Occupations with Highest Median Age, 2006

Occupation	Median Age 2001	Median Age 2006	Employment Level in 2006	Percentage aged 55 years and older in 2006
Farmers and farm managers	51.1	51.9	197,800	42.3
Real estate agents and salespersons	49.9	50.7	61,100	36.5
Property administrators	48.9	50.2	42,900	36.1
Bus drivers and transit operators	48.8	50.1	29,400	36.3
Ministers of religion	47.7	50.1	76,700	33.9
Senior managers (health, education, social and community services)	47.8	50.0	21,500	29.7
Senior government managers	48.1	49.7	20,900	25.5
School principals and administrators	49.8	49.4	28,700	24.3
Senior managers (goods, utilities, transportation, construction)	47.0	48.8	59,800	29.2
University professors	48.5	48.7	54,400	31.8

Source: Statistics Canada, *Canada's Changing Labour Force*, 2006 Census, p. 25.

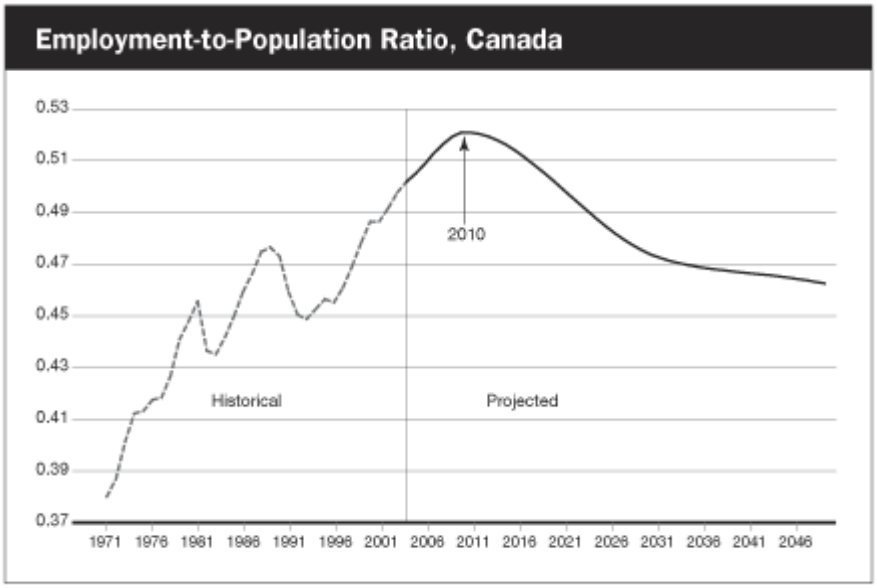
Data from the 2006 Census indicate that the number of people in the labour force increased by 1.3 million between 2001 and 2006. The data also show that Canada's workforce is aging: those aged 55 and older accounted for 15.3% of the total labour force in 2006, up from 11.7% in 2001. The median age of the labour force was above 40 years for the first time ever: the median age was 41.2 years in 2006, up from 39.5 years in 2001.[11] Occupations such as farmers, real estate agents, property administrators, bus

11 Statistics Canada, *Canada's Changing Labour Force*, 2006 Census.

drivers, ministers of religion, and senior managers in the private and public sectors have particularly high median ages (see Table 1). Many of these occupations are found in the services sector.

The combination of an aging population, a lower retirement age, fewer young people entering the working-age population, increased demand for workers with specialized skills, and international worker mobility has led (or may lead) to labour shortages in some areas of the economy.[12] Moreover, Finance Canada expects Canada's employment-to-population ratio to turn negative in 2010, as growing numbers of "baby boomers" retire (see Figure 18).[13] Somewhat in response, Canada has increasingly turned to immigration as a source of skilled labour. Data from the 2006 Census indicate that about 3.6 million individuals in the labour force were foreign born. Foreign-born individuals thus account for more than one-fifth (21.2%) of Canada's total labour force of about 17.1 million people in 2006, up from 19.9% in 2001.[14]

Figure 18



Source: Department of Finance calculations.

12 Canada's population is aging due to a prolonged period of low fertility and increasing life expectancy. Fertility in Canada has been declining since the 1960s; the fertility rate was 3.9 children per woman in 1956 and, currently, it stands at 1.7, which is significantly below the replacement rate of 2.1. Given this performance, births in Canada peaked in 1990, trending downward ever since. Canadians, on average, lived 80.1 years in 2005, up 11 years from 69.1 years in the 1950-1955 period. The source of the cited data is Human Resources and Skills Development Canada, Policy Research Initiative Project: Population Aging and Life-Course Flexibility, Encouraging Choice: Aging, Labour Supply and Older Workers, briefing note, November 2005.

13 Finance Canada, *Budget 2005*, Annex 3, Canada's Demographic Challenge, p. 296-311.

14 Statistics Canada, *Canada's Changing Labour Force*, 2006 Census, p. 29.

The rapid and significant appreciation in the value of the Canadian dollar since 2002 has made many manufacturers less competitive relative to foreign competitors. They have had to both reduce employment and invest in capital machinery and equipment to raise their labour productivity levels in order to stabilize their production levels and relative competitiveness. Given that national employment levels have risen to all-time highs and national unemployment rates have declined to modern day lows (i.e., lowest levels in 33 years), other goods-producing sectors and services sectors are engaging many of the skilled workers laid-off by the manufacturing sector.

In part because of this uneven economic performance across major sectors of the economy, employment growth has been uneven across the country. National employment averaged 16 million in 2006, up 1.3 million from 2001. Two provinces — Alberta and British Columbia — accounted for about one third of this increase. Moreover, the unevenness of employment growth across the country also stimulated considerable migration. According censuses data, 562,800 employed people or 3.4% of the labour force moved to a different province or territory between 2001 and 2006. The three northern territories, followed by Alberta, had the highest shares of people from another province making up their labour force.

Focusing on Canada's services sector, employment approached 12.9 million in 2007, and has grown on average by 2.4% per annum between 2002 and 2007, accounting for almost 93% of the increase in total employment in Canada between 2002 and 2007. Many industries across the services sector report current or anticipated difficulties in hiring and retaining staff. Indeed, such problems are likely to become more pronounced as demographic changes lead to a shrinking labour force.

The Committee recognizes that slower economic growth induced by a labour skills shortage can be mitigated or countered by taking actions to: (1) increase the participation rate of those not fully participating in the labour force; (2) increase the value of work performed per person of those already in the labour market; and/or (3) increase the skill levels of those entering the labour force.

In the hope of reducing some of the barriers to re-entering the labour market by selected groups who have either completely or partially withdrawn from the labour market, most notably low-income individuals and seniors, the Committee recommends:

That the Government of Canada continue reforming fiscal policies that discourage work by:

(1) expanding the working tax credit for low-income individuals;

(2) reducing the claw-back rate for seniors on Guaranteed Income Supplement (GIS) and Employment Insurance (EI) recipients who return to the labour force; and

(3) reducing the statutory personal income tax rate.

Other notable groups who are not fully participating in the labour force include new parents. Child care for children aged six months to five years is utilized by most Canadian parents, and use rates are increasing. In 2003, 52% of children from two-parent households and 64.4% of children in single parent households were cared for by someone other than a family member, an increase from 42% and 39%, respectively, from 1995.[15] Rates of daycare use varied by province: Alberta being the lowest (46%) and Quebec being the highest (70%). Cost to parents also varies by province from an average of $205 per month in Quebec to $800 in Ontario. The Committee, therefore, recommends:

> **That the Government of Canada work with the provincial and territorial governments to implement early childcare and early learning systems with the aim of reducing barriers to parents, particularly women, who choose to be in the workforce.**

In the hope of increasing the value of work performed per person of those already in the labour market, the Committee first focuses on the plight of recent immigrants to Canada. It is far too often the case that immigrants to Canada may have professional qualifications, for example in the healthcare, engineering, or education fields, but the time taken to recognize their foreign credentials may delay by a considerable length of time their right to begin work in their chosen profession in Canada. This situation leaves Canada at a disadvantage when highly qualified professionals are in short supply. The Committee, therefore, recommends:

> **That the Government of Canada work with the provinces and professional organizations to streamline the entry of foreign workers into the labour force, with the goal to commence, and if possible to complete, the process of recognition of foreign credentials in the country of origin.**

The Committee now focuses on other existing labour market participants who could raise their skill levels and assist in reducing any impending skills shortage. The reallocation of labour necessitated by industrial restructuring and a relatively high-valued Canadian dollar has, in some cases, been insufficient in terms of the number of potential employees available or in matching skill sets with demand, and has prohibited some companies and industries from meeting rising demand for their services. Improving employee skills through on-site training or by sending employees to training programs are ways for firms to deal with a lack of skilled labour. Employees with enhanced skills not only help the company providing the training, but they are more marketable in the long term, and less likely to draw Employment Insurance, or to draw it for shorter periods of time, in the future.

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15 Statistics Canada, *The Daily, Child care: An eight-year profile*, 5 April 2006, http://www.statcan.ca/Daily/English/060405/d060405a.htm.

The cost of paying for training and temporarily losing employees while they are participating in training activities often prohibits companies, especially small and medium-sized enterprises, from providing training to their employees. Furthermore, since employees that have upgraded their skills are more marketable, they may seek other, more lucrative employment opportunities, especially in tight labour markets, once their training is complete; the company providing the training may therefore reap little or no benefit from the training for which it has paid. To address this problem, the Committee recommends:

> **That the Government of Canada provide tax credits and/or other measures to companies providing employer-financed training and apprenticeships to their employees.**

Taxation Policy

Tax relief in various forms was suggested by most witnesses and was not limited in its application to the services sector. The suggested tax measures were most often meant to address their existing or impending labour shortage problems and skills development shortcomings. These issues were addressed by the Committee in the preceding section. By far the next most controversial tax issue mentioned by witnesses stemmed from inefficiencies resulting from two sales tax regimes (federal versus provincial). Some witnesses suggested further reductions in corporate income tax rates as a means of spurring economic activity. Finally, one witness suggested the introduction of income averaging provisions to the federal income tax system to provide tax relief for individuals with highly variable incomes.

Beginning with Canada's income tax regime and the cultural industry's call for an income averaging provision — possibly similar to that which prevailed in the 1970s — the Committee looks first to the issue of equity, followed by fiscal or budgetary issues.

Canada's federal income tax system imposes higher tax rates on annual income that falls within higher income tax brackets. For many, the progressive structure of Canada's income tax system ensures a fair distribution of the tax burden according to one's ability to pay, thereby satisfying so-called "vertical equity" concerns. One unintended consequence of a progressive tax system that is based on annual income, however, is that an individual with variable annual income may end up paying more taxes than an individual with stable income even though the two individuals earn the same income over a period of several years. In this case, the principle that people earning the same level of income should face the same tax burden is violated because the income tax system is based on annual income, and the choice of "annual income" over daily, weekly, monthly, biennial or triennial income is simply a matter of convention and convenience. Convention, convenience and "vertical equity" concerns thus appear to trump "horizontal equity" concerns in the case of variable annual incomes under Canada's current progressive annual income tax system.

In 1973, the *Income Tax Act* introduced a general averaging provision that was made available to taxpayers whose income in a particular taxation year was 10% higher than their prior year's income and 20% higher than the average of their annual income for the four preceding years.[16] This general averaging provision was eliminated in 1982 and was replaced with a forward income-averaging mechanism available to all taxpayers, only to see it gradually phased-out starting in 1988. The Department of Finance estimated that the general averaging provision cost the federal government $350 million in foregone revenue for the 1980 calendar year.[17] When adjusted for inflation and the number of tax returns, this cost estimate would be approximately $1.5 billion in foregone revenue for the federal government for the 2006 calendar year.

The Committee believes that Canada's tax regime must provide equity to individuals with variable incomes through similar treatment to individuals with stable incomes and, therefore, recommends:

That the Government of Canada introduce measures into the income tax system that would allow self-employed Canadians with highly variable incomes to average their incomes over several years.

The Committee also agrees with the witnesses who suggested further reductions in corporate income tax rates as a means of spurring economic activity and productivity growth. The Committee, therefore, recommends:

That the Government of Canada continue to reduce the federal corporate tax rate.

Moving on to Canada's Goods and Services Tax (GST), many witnesses suggested that the government should: (1) harmonize the GST with provincial retail sales taxes; (2) reinstate the GST rebate for foreign visitors; and (3) remove the GST from books.

The rationale for reinstating the former rebate on the GST for foreign visitors is to provide indirect financial assistance to the tourism industry that has been particularly hit hard by the large and rapid ascent of the Canadian dollar, high fuel prices, lengthy wait times at the border, confusion surrounding passport requirements and a relative shift towards more exotic holiday destinations. Canada has seen a decrease in international tourists from 40.9 million in 2003 to 28.9 million in 2006. Consequently, Canada's tourism trade deficit has grown from $1.7 billion in 2002 to $7.2 billion in 2006 and is expected to be more than $8 billion in 2007. The Committee, therefore, recommends:

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16 The general averaging provision was phased in, so the number of applicable preceding years was one year in 1973, two years in 1974 and three years in 1975. Furthermore, incomes for the purpose of the scheme could not fall bellow a certain threshold: $1,700 in 1973 and from then on was indexed to the cost of living.

17 Department of Finance, "Government of Canada Tax Expenditure Accounts," December 1980.

That the Government of Canada reinstate the Goods and Services Tax (GST) rebate for foreign visitors and promote this rebate to visitors upon entry into Canada.

Finally, the rationale for removing the GST on books is to reduce financial barriers to literacy. The Committee, therefore, recommends:

That the Government of Canada remove the Goods and Services Tax (GST) on books.

Innovation, Intellectual Property and Technology Policies

Innovation often underlies the ability of Canada's services sector to grow and compete internationally. Whether it is new processes resulting from intensive research and development, enhanced training or education, data storage, improved regulations or deregulation, or a new design and marketing strategy, innovation makes services sector firms a better place to work, more effective in providing services to Canadians, and more competitive against foreign rivals. In order to remain at the cutting edge of developing and implementing services sector innovations, the Committee recommends:

That the Government of Canada develop a services sector innovation strategy.

The Committee understands that business R&D intensity (expenditure relative to industry's contribution to GDP) in Canada is lower than the OECD average, and that the business sector funds and performs a lower percentage of R&D to total national R&D than does the business sector of other OECD countries. Consequently, the Government of Canada supports industrial research and development (R&D) in a number of ways, including the Scientific Research and Experimental Development (SR&ED) Tax Incentive Program.

Canada's SR&ED program is one of the most advantageous in the industrialized world, providing more than $2.6 billion in deductions or credits to Canadian businesses in 2005. The tax incentives for SR&ED come in two forms: (1) income tax deductions; and (2) investment tax credits (ITCs) for SR&ED conducted in Canada. In terms of income tax deductions, current expenditures (e.g., salaries of employees directly engaged in SR&ED, the cost of materials consumed in SR&ED, overhead) and capital expenditures on machinery and equipment are fully deductible in the year incurred. Unused deductions may be carried forward indefinitely. In terms of ITCs, there are two rates under SR&ED:

- the general rate of 20%; and

- an enhanced credit rate of 35% for smaller Canadian-controlled private corporations (CCPCs) on their first $3 million of eligible expenditures; these ITCs are refundable to smaller CCPCs at a rate of 100% on current expenses and 40% on capital expenses.

ITCs may be deducted from federal taxes otherwise payable. Unused ITCs may be carried back three years or carried forward 20 years.

The Committee deliberated on a number of suggestions for change to the SR&ED tax incentive program, including:

- making the SR&ED investment tax credits refundable;

- excluding SR&ED investment tax credits from the calculation of the tax base;

- providing an allowance for international collaborative research and development; and

- expanding the SR&ED investment tax credits to cover the costs of patenting, prototyping, product testing and other pre-commercialization activities.

Finance Canada concludes that the cost of extending full refundability of SR&ED ITCs to all firms and all types of expenditures would depend on the treatment of existing pools and unused ITCs. Depending on whether the application of ITC pools to current taxes would affect the refund available, the fiscal cost of refundability is estimated to be between $5 billion and $10 billion over five years.

Finance Canada concludes that the cost of excluding SR&ED ITCs from the tax base would depend on whether the proposal would apply only to federal ITCs, or include provincial ITCs for R&D, and whether the change in allowable expenditures for the purpose of the tax deduction would also flow through to qualified expenditures for the ITCs. Depending on how the change is implemented, the fiscal cost is estimated to be between $1 billion and $4 billion over five years.

Finance Canada concludes that the cost of providing an allowance for international collaborative R&D would depend on the definition of this activity and the type of allowance provided. Based on Statistics Canada data on industrial payments for R&D and other technical services abroad, and assuming the allowance would be provided by including expenditures for such activities in the base for the ITC, the fiscal cost of this proposal is estimated to be $2.2 billion over five years.

Finance Canada did not provide an estimate on extending the tax credit to cover patenting, prototyping, product testing, and other pre-commercialization activities because there was no data readily available on the size of corporate expenditures on these items. Therefore, excluding the proposal to extend the tax credit to cover these other activities, the fiscal cost of implementing the above SR&ED measures would vary from $8.2 billion to $16.2 billion over five years. However, given the extent of the fiscal costs and the as-of-yet non-quantified social and fiscal benefits associated with the above suggested changes, the Committee recommends:

> **That the Government of Canada improve the Scientific Research and Experimental Development (SR&ED) Tax Incentive Program to make it more accessible and relevant to Canadian businesses.**

The Committee made a similar recommendation in its previous report dealing with the manufacturing sector, entitled *Manufacturing: Moving Forward — Rising to the Challenge*,[18] and was given a positive response by the government.[19] The Committee, therefore, awaits the government's final conclusions and decision on potential changes to the SR&ED tax incentive program.

Critical support for some innovations — often the result of R&D — is provided by intellectual property law. Intellectual property laws confer a bundle of exclusive rights upon authors and inventors for a limited period, allowing them to better exploit their works and invention. The rationale for the creation of such rights is that they facilitate and encourage the pursuit of innovation (i.e., increase the profitability associated with innovation by discouraging unauthorized copies from entering the marketplace and competing with the original) and the disclosure of knowledge into the public domain for the common good (i.e., thereby reducing secrecy as a profit-making strategy and permitting others to improve upon the innovation). The intellectual property (IP) right is the only industrial tool that rewards the innovator commensurate with the innovation's commercial prospects.

In Canada, the following federal laws and regulations, which are administered by the Canadian Intellectual Property Office (with the exception of the *Plant Breeders' Rights Act*), relate to the protection of IP:[20]

- *Patent Act*;

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18 House of Commons Standing Committee on Industry Science and Technology, Fifth Report, *Manufacturing: Moving Forward – Rising to the Challenge*, February 2007, http://cmte.parl.gc.ca/Content/HOC/committee/391/indu/reports/rp2663393/indurp05/indurp02-e.pdf.

19 Department of Finance Canada, *The Budget Plan 2007: Aspire to a Stronger, Safer, Better Canada*, March 19, 2007, http://www.budget.gc.ca/2007/pdf/bp2007e.pdf.

20 Industry Canada, Intellectual Property Policy Directorate, Laws and Regulations, http://www.strategis.ic.gc.ca/epic/site/ippd-dppi.nsf/en/h_ip00007e.html.

- *Patented Medicines (Notice of Compliance) Regulations*;
- *Copyright Act*;
- *Trade-marks Act*;
- *Industrial Design Act*;
- *Integrated Circuit Topography Act*; and
- *Plant Breeders' Rights Act*.

In terms of controlling counterfeiting and piracy specifically, other pertinent federal legislation includes the *Food and Drugs* Act, the *Customs Act*, the *Canada Border Services Agency Act* and the *Criminal Code*.

Counterfeiting and piracy affect the services industry in many ways, including the loss in sales in the retail sector of the legitimate product, loss of revenues in entertainment through film piracy, and lower levels of research and development. In particular, the Committee heard that in some cases (e.g., Microsoft products) levels of software piracy are above 33%. The Committee views trademark counterfeiting and copyright piracy as a drain on the Canadian economy, and, in the case of some counterfeit goods, as a threat to public health and safety. The Committee, therefore, recommends:

That the Government of Canada vigorously enforce intellectual property, anti-counterfeiting and anti-piracy legislation.

Access to the latest information technology can give small businesses across the services sector an advantage. Whether used for inventory control in the retail sector, communications in the financial and insurance sector, research and development, the latest publishing or editing tools, or other industries, information technology can increase productivity and reduce costs. However, investments in information technology can be expensive and their payback periods may be long. The Committee, therefore, recommends:

That the Government of Canada introduce an information technology investment tax credit for small businesses.

Internal Trade Policies

Unimpeded labour mobility is an important component of an efficient labour market. The Agreement on Internal Trade (AIT), signed in 1994, requires that provinces and

territories eliminate barriers to labour mobility such as residency requirements for registration and unnecessary fees and delays. It also requires governments to mutually recognize the qualifications of workers already qualified in other provinces/territories, reconcile differences in occupational standards, and put in place accommodation mechanisms to help workers acquire any additional competencies they need related to differences in scope of practice across jurisdictions.

Despite this agreement, there continue to be inter-provincial barriers to labour mobility; progress is being made in removing these barriers but it has been slow. In September 2006, the Committee of Federal-Provincial-Territorial Ministers Responsible for Internal Trade came to an agreement on an action plan on internal trade. A key component of the action plan is a strategy to improve labour mobility so that by April 1, 2009, Canadians will be able to work anywhere in Canada without restrictions on labour mobility (i.e., full compliance with the labour mobility provisions of the AIT). The Committee supports:

> **Agreements recently concluded on construction labour mobility between Quebec and Ontario and on trade, investment and labour mobility signed by Alberta and British Columbia. The Committee believes that removing all additional barriers to labour mobility within Canada is an important means of dealing with regional shortages of skilled labour and ultimately leads to a better allocation of labour within the country.**

The Committee also intends to undertake a study of these inter-provincial barriers in the near future, but until such time the Committee recommends:

> **That the Government of Canada should take a leadership role and encourage the provinces to bring down inter-provincial trade, investment and labour mobility barriers.**

Regulatory Policy

Governments use regulation in combination with other instruments, such as taxation, program delivery and services, and voluntary standards to achieve public policy objectives. Regulations can be beneficial to businesses by creating an environment in which commercial transactions take place in predictable ways, consistent with the rule of law. Complying with regulations can, however, be a costly endeavour, and hits small businesses particularly hard. The Committee believes that, in certain cases, regulation is excessive or duplicative, and that in these cases, regulation is impeding innovation or productivity.

One such example was provided to the Committee by representatives of the retail sector involving the movement of foreign-based marine containers. Unlike in the United

States, Canadian regulations (i.e., Customs Tariff 9801.10.00) require incoming (foreign-based) marine containers to exit via the same port within 30 days, and they must return empty rather than be refilled in order to ensure duty-free treatment. The Committee is unsure of the social objectives that these rules are meant to achieve, but understands very clearly both the added costs imposed on retailers from adopting regulations that breed inefficient transportation and distribution methods, as well as their adverse environmental implications. The Committee, therefore, recommends:

> **That the Government of Canada study and review regulations that govern the movement of marine containers (i.e., cabotage regulations) such as the requirement that incoming containers exit via the same port within 30 days.**

Infrastructure Policy

The services sector needs access to modern infrastructure to allow the continued growth of the sector. This includes transportation, water and sewage, and telecommunications infrastructure. The retail, food and restaurant sectors depend on transportation infrastructure to ship goods. The travel and tourism industries depend on transportation infrastructure. The information technology and the financial services industries rely on an effective telecommunications infrastructure, and the Committee heard from the insurance industry on the need to renew water and sewage infrastructure to minimize the risk of catastrophic flood events. As such, the Committee recommends:

> **That the Government of Canada increase efforts in partnership with the provinces and municipalities to invest in transportation, water and sewage infrastructure.**

National Border Policy

A border or immigration official is often the first Canadian a visitor to Canada will speak with on their arrival in the country, and his or her demeanour provides a first, and sometimes lasting, impression of Canada. The Committee recognizes the professionalism of border and immigration officials, their role in protecting the Canadian public, and the need for them to maintain vigilance at all times. Whilst carrying out those duties, border and immigration official have a unique opportunity to give visitors a positive first impression of Canada, enhancing the visitors experience, as well as welcoming back returning Canadians. The Committee, therefore, recommends:

> **That the Government of Canada encourage border and immigration officials to be welcoming to people entering Canada.**

Canada's business sector — most notably, the tourism industry — is particularly concerned about continued delays at certain border crossings into the United States. The Windsor-Detroit Corridor is Canada's most important entry to the United States, with 28% of goods shipments between Canada and the United States passing through that corridor. Congestion at this crossing has a negative impact on Canada's economy. The Committee, therefore, recommends:

> **That the Government of Canada continue to invest substantially in infrastructure to reduce delays at Canada-U.S. border crossings and all points of entry, and ensure new passport rules are implemented seamlessly.**

International Trade Policy

Although services make up three quarters of domestic commercial activity, they account for a much smaller proportion of international trade. In 2007, services accounted for only 13% of exports and 17% of imports. The Department of Foreign Affairs and International Trade, through its Trade Commissioner Service at foreign missions, promotes and facilitates trade between Canada and international partners. In order to fully exploit opportunities to enhance international trade in the services sector, the Committee recommends:

> **That the Government of Canada continue to ensure that staff in foreign missions has the expertise, knowledge and resources to promote the services sector.**

As a trading nation, Canada remains committed to multilateral trade and its rules-based system that underpins commercial relations with the 148 other member countries of the World Trade Organization (WTO). Canada's first priority on matters of trade continues to be the enhancement of the multilateral trade system, including the conclusion of an agreement based on the "Doha Development Agenda" launched in November 2001. As part of its prosperity initiative, Canada has also negotiated a bilateral free trade agreement with Chile, Costa Rica, Israel and the United States and a regional free trade agreement with Mexico and the United States. The Committee, therefore, recommends:

> **That the Government of Canada seek further favourable and comprehensive bilateral and multilateral trade agreements that would include services sector obligations.**

As established in its November 2006 policy statement, entitled *Blue Sky: Canada's International Air Policy*, the Government of Canada will proactively pursue opportunities to negotiate more liberalized agreements for international scheduled air transportation that will provide maximum opportunity for passenger and all-cargo services to be added according to market forces. More specifically, Canada will seek to negotiate reciprocal "Open Skies"-

type agreements similar to the one negotiated with the United States in November 2005, where it is deemed to be in Canada's overall interest. According to the Government of Canada, an "Open Skies"-type agreement would cover the following elements for scheduled passenger and all-cargo services:

- open bilateral markets/access (third and fourth freedom rights);
- no limit on the number of airlines permitted to operate;
- no limits on the permitted frequency of service or aircraft type;
- market-based tariff/pricing regime for bilateral and third-country services;
- open and flexible regime for the operation of code-sharing services;
- unrestricted services to and from third-countries (fifth and sixth freedom rights); and
- rights for stand-alone all-cargo operations (seventh freedom rights).

Under no circumstances will the policy approach include cabotage rights — the right for a foreign airline to carry domestic traffic between points in Canada (eighth and ninth freedom rights). The Committee agrees and, therefore, recommends:

> **That the Government of Canada pursue more open skies agreements to the benefit of Canadians.**

Cultural Policy

The Canadian Radio-television and Telecommunications Commission (CRTC) has established a quota system to regulate the amount of Canadian content (also known as Cancon) on radio, television and specialty broadcasting based on its mandate provided under the *Broadcasting Act* which stipulates that:[21]

> The Canadian broadcasting system should:
>
> (i) serve to safeguard, enrich and strengthen the cultural, political, social and economic fabric of Canada,

21 Canadian *Broadcasting Act*, http://laws.justice.gc.ca/en/ShowFullDoc/cs/B-9.01///en.

(ii) encourage the development of Canadian expression by providing a wide range of programming that reflects Canadian attitudes, opinions, ideas, values and artistic creativity, by displaying Canadian talent in entertainment programming and by offering information and analysis concerning Canada and other countries from a Canadian point of view.

Requirements for Canadian content vary by broadcast medium: 35% of music on commercial radio stations must be Canadian, and 60% of television shows must be Canadian. For music to qualify as Canadian content, it should be composed, written or performed by a Canadian, or should be performed or recorded in Canada. For television programming evaluation is made on the basis of whether creative personnel are Canadian, and the amounts paid to Canadian to produce the program.

There are also guidelines under the *Investment Canada Act* governing Canadian content in magazines to ensure "the availability to Canadians of periodicals that are relevant to Canadian life and culture, reflect an identifiably Canadian perspective and meet the information needs of Canadian readers."[22] In general, foreign investments in periodicals are reviewed to ensure there will be a majority of original Canadian content authored by Canadian writers, journalists, illustrators or photographers, or content created solely for the Canadian market.

Telecommunications, cable-television and satellite television companies, by contrast, are governed by foreign ownership restrictions set out in the *Telecommunications Act* and the *Broadcasting Act*. Direct foreign ownership in such companies cannot exceed 20% of the share capital of the corporation. In addition, according to *Canadian Telecommunications Common Carrier Ownership and Control Regulations*, the minimum Canadian ownership level for ownership at the holding company level is 66⅔% of voting shares. This caps foreign ownership in a telecommunications common carrier and a broadcast distribution undertaking (BDU) at 46⅔%.[23] The Committee agrees with these restrictions and recommends:

That the Government of Canada increase efforts to provide regulation that promote Canadian ownership and Canadian content in media.

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22 Heritage, Cultural Sector Investment Review, *Canadian Content in Magazines: A Policy on Investment in the Periodical Publishing Sector*, www.canadianheritage.gc.ca/progs/ac-ca/progs/eiic-csir/period_e.cfm (accessed December 5, 2007).

23 The 66⅔% minimum level for Canadian ownership means that a foreign company that holds 20% of the voting stock of a Canadian telephone operating company could also have a 33⅓% stake in a company that held the remaining 80% voting stock of the Canadian telephone operating company. Multiplying 33⅓% by 80% and adding 20% leads to the current aggregate direct and indirect foreign ownership limit of 46⅔%.

Health Care Policies

Inaccessibility to services was cited as the main challenge in health care services. In the publicly funded health care field, inaccessibility and long wait times are caused by too few health care professionals or lack of equipment. The Canadian Medical Association (CMA) estimates the cumulative cost of waiting for joint replacement, cataract surgery, heart bypass grafts and MRI scans is $14.8 billion. The CMA also estimates that almost 5 million Canadians do not have access to a family physician. Canada ranks twenty-fourth among OECD countries in terms of physicians-per-population ratio and would need 26,000 more doctors to meet the OECD average. In private care such as dentistry, problems with access are generally caused by high fees, with some Canadians unable to pay for the high cost of treatment and therefore going without care.

The Canadian Healthcare Association made a number of interesting suggestions and this Committee finds itself in agreement with some of them. The Committee, therefore, recommends:

> **That the Government of Canada ensure health care workers offering services to First Nations, Inuit and Métis people be appropriately culturally educated; and**
>
> **That the Government of Canada work with provincial and territorial governments to improve the retention of health care workers providing services to First Nations, Inuit and Métis.**

CONCLUSION

There have been at least two dominant economic forces driving structural change of the Canadian economy. Firstly, for more than five decades, the demand for services by Canadians has been growing rapidly, both in absolute terms and relative to that of goods. Secondly, for more than five years, a worldwide "commodities boom" has directly and indirectly forced a restructuring of the economy towards the natural resources and services sectors and away from the manufacturing sector. Together, these two economic forces have been positive for Canada: wealth has been on the rise and the economy has been expanding at breakneck speed since 2002. This economic growth has been widespread throughout the Canadian economy, services-producing and goods-producing sectors alike, except for Canadian-dollar-sensitive industries such as manufacturing and tourism. In turn, employment across Canada has been growing; job creation has been spectacular; and both Canada's employment rate and unemployment rate have respectively set a 33-year high/low in the process.

Activity levels and employment in Canada's services sector have also enjoyed long-term robust growth. The services sector has grown, on average, a half of a percentage point more than the overall economy each year since 2002, and accounts for almost 70% of total Canadian economic activity in 2007. Employment in the services sector has also grown, on average, by 2.4% per annum since 2002, and now accounts for more than 75% of total Canadian employment. Indeed, the services sector accounted for almost 93% of the increase in employment in Canada between 2002 and 2007.

Canada's services sector is not without its challenges, however. The sector faces and will increasingly face a labour skills shortage as Canada's population ages, the rate of retirement increases, and the labour force shrinks. According to Finance Canada, Canada's employment-to-population ratio is going to turn negative in 2010, as growing numbers of "baby boomers" retire. As such, the Committee recognizes that slower economic growth induced by a shrinking labour market and a labour skills shortage can be mitigated or countered by taking actions to: (1) increase the participation rate of those not fully participating in the labour force; (2) increase the value of work performed per person of those already in the labour market; and/or (3) increase the skill levels of those entering the labour force. The Committee makes a number of public policy recommendations to address the labour skills challenge that will provide economic benefits beyond the services sector.

Services sub-sectors such as tourism, information and communications technologies, culture, health care and retail trade also face industry-specific challenges, and the Committee has recommended a number of targeted tax measures for dealing with each of their specific challenges. In the end, the Committee believes that the Government of Canada's timely implementation of these recommendations — timely in the sense of when the federal fiscal situation permits — will help to ensure continued growth and prosperity of Canada's services sector.

LIST OF RECOMMENDATIONS

RECOMMENDATION 1: (p. 41)

That the Government of Canada continue to improve Statistics Canada's collection and dissemination of data on the services sector.

RECOMMENDATION 2: (p. 41)

That the Government of Canada move the responsibility for the Co-operatives Secretariat from Agriculture Canada to Industry Canada.

RECOMMENDATION 3: (p. 44-45)

That the Government of Canada continue reforming fiscal policies that discourage work by:

(1) expanding the working tax credit for low-income individuals;

(2) reducing the claw-back rate for seniors on Guaranteed Income Supplement (GIS) and Employment Insurance (EI) recipients who return to the labour force; and

(3) reducing the statutory personal income tax rate.

RECOMMENDATION 4: (p. 45)

That the Government of Canada work with the provincial and territorial governments to implement early childcare and early learning systems with the aim of reducing barriers to parents, particularly women, who choose to be in the workforce.

RECOMMENDATION 5: (p. 45)

That the Government of Canada work with the provinces and professional organizations to streamline the entry of foreign workers into the labour force, with the goal to commence, and if possible to complete, the process of recognition of foreign credentials in the country of origin.

RECOMMENDATION 6: (p. 46)

That the Government of Canada provide tax credits and/or other measures to companies providing employer-financed training and apprenticeships to their employees.

RECOMMENDATION 7: (p. 47)

That the Government of Canada introduce measures into the income tax system that would allow self-employed Canadians with highly variable incomes to average their incomes over several years.

RECOMMENDATION 8: (p. 47)

That the Government of Canada continue to reduce the federal corporate tax rate.

RECOMMENDATION 9: (p. 48)

That the Government of Canada reinstate the Goods and Services Tax (GST) rebate for foreign visitors and promote this rebate to visitors upon entry into Canada.

RECOMMENDATION 10: (p. 48)

That the Government of Canada remove the Goods and Services Tax (GST) on books.

RECOMMENDATION 11: (p. 48)

That the Government of Canada develop a services sector innovation strategy.

RECOMMENDATION 12: (p. 50)

That the Government of Canada improve the Scientific Research and Experimental Development (SR&ED) Tax Incentive Program to make it more accessible and relevant to Canadian businesses.

RECOMMENDATION 13: (p. 51)

That the Government of Canada vigorously enforce intellectual property, anti-counterfeiting and anti-piracy legislation.

RECOMMENDATION 14: (p. 51)

That the Government of Canada introduce an information technology investment tax credit for small businesses.

RECOMMENDATION 15: (p. 52)

That the Government of Canada should take a leadership role and encourage the provinces to bring down inter-provincial trade, investment and labour mobility barriers.

RECOMMENDATION 16: (p. 53)

That the Government of Canada study and review regulations that govern the movement of marine containers (i.e., cabotage regulations) such as the requirement that incoming containers exit via the same port within 30 days.

RECOMMENDATION 17: (p. 53)

That the Government of Canada increase efforts in partnership with the provinces and municipalities to invest in transportation, water and sewage infrastructure.

RECOMMENDATION 18: (p. 53)

That the Government of Canada encourage border and immigration officials to be welcoming to people entering Canada.

RECOMMENDATION 19: (p. 54)

That the Government of Canada continue to invest substantially in infrastructure to reduce delays at Canada-U.S. border crossings and all points of entry, and ensure new passport rules are implemented seamlessly.

RECOMMENDATION 20: (p. 54)

That the Government of Canada continue to ensure that staff in foreign missions has the expertise, knowledge and resources to promote the services sector.

RECOMMENDATION 21: (p. 54)

That the Government of Canada seek further favourable and comprehensive bilateral and multilateral trade agreements that would include services sector obligations.

RECOMMENDATION 22: (p. 55)

That the Government of Canada pursue more open skies agreements to the benefit of Canadians.

RECOMMENDATION 23: (p. 56)

That the Government of Canada increase efforts to provide regulation that promote Canadian ownership and Canadian content in media.

RECOMMENDATION 24: (p. 57)

That the Government of Canada ensure health care workers offering services to First Nations, Inuit and Métis people be appropriately culturally educated; and

RECOMMENDATION 25: (p. 57)

That the Government of Canada work with provincial and territorial governments to improve the retention of health care workers providing services to First Nations, Inuit and Métis.

APPENDIX A
LIST OF WITNESSES

Organizations and Individuals	Date	Meeting
Department of Finance	2007/11/22	4
Colleen Barnes, Acting Director, Financial Institutions, Financial Sector Policy Branch		
Department of Industry		
Janet King, Director General, Service Industries and Consumer Products Branch		
Tom Wright, Assistant Deputy Minister, Industry Sector		
Canadian Bankers Association	2007/11/27	5
Terry Campbell, Vice-President, Policy		
Nancy Hughes Anthony, President and Chief Executive Officer		
Canadian Life and Health Insurance Association Inc.		
Yves Millette, Senior Vice-President, Quebec Affairs		
Frank Swedlove, President		
James Witol, Vice-President, Taxation and Research		
Insurance Bureau of Canada		
Mark Yakabuski, President and Chief Executive Officer		
Canadian Restaurant and Foodservices Association	2007/11/29	7
Ron Reaman, Vice-President, Federal		
Joyce Reynolds, Executive Vice-President, Government Affairs		
Retail Council of Canada		
Diane Brisebois, President and Chief Executive Officer		
Kim Furlong, Director, Government Relations		
Hotel Association of Canada	2007/12/04	8
Anthony Pollard, President		
Tourism Industry Association of Canada		
Christopher Jones, Vice-President, Public Affairs		
Randy Williams, President and Chief Executive Officer		
IBM Canada	2007/12/06	10
Matthew Ivis, Governmental Programs Executive		
Information Technology Association of Canada		
Bernard Courtois, President and Chief Executive Officer		

Organizations and Individuals	Date	Meeting
Microsoft Canada Co.	2007/12/06	10
Marc Seaman, National Director, Corporate and Public Affairs		
Alliance of Canadian Cinema, Television and Radio Artists (ACTRA)	2007/12/11	11
Richard Hardacre, National President		
Campus Stores Canada		
Chris Tabor, Board Representative		
Canadian Booksellers Association		
Susan Dayus, Executive Director		
Design Exchange		
Samantha S. Sannella, President and Chief Executive Officer		
Canadian Association of Management Consultants	2007/12/13	13
Bob McCulloch, Vice-Chair		
Heather Osler, President and Chief Executive Officer		
Conference Board of Canada		
Glen Hodgson, Senior Vice-President and Chief Economist		
Canadian Co-operative Association	2008/01/29	14
John Anderson, Director, Government Affairs and Public Policy		
Carol Hunter, Executive Director		
Canadian Council of Chief Executives		
Sam Boutziouvis, Vice-President, Economics and International Trade		
David Stewart-Patterson, Executive Vice-President		
Canadian Services Coalition		
Shirley-Ann George, Executive Director		
Hon. Sergio Marchi, Chair		
Conseil canadien de la coopération		
Brigitte Gagné, Executive Director		
Toronto Association of Business Improvement Areas		
Michael Comstock, Vice-President		
Air Transport Association of Canada	2008/01/31	16
Sam Barone, President and Chief Executive Officer		
Fred Gaspar, Vice-President, Policy and Strategic Planning		
Canadian Trucking Alliance		
Graham Cooper, Senior Vice-President		
Ron Lennox, Vice-President, Trade and Security		

Organizations and Individuals	Date	Meeting
Export Development Canada	2008/01/31	16
Stephen Poloz, Senior Vice-President and Chief Economist, Corporate Affairs		
SNC-Lavalin Group Inc.		
Robert Blackburn, Senior Vice-President, Government and International Development Institutions		
Supply Chain and Logistics Association Canada		
Bob Armstrong, President		
BIOTECanada	2008/02/05	17
Joanne Harack, Co-Chair, Public Affairs Committee		
Cate McCready, Vice-President, External Affairs		
Canadian Advanced Technology Alliance		
Eli Fathi, Vice-President, Commercialization		
Barry Gander, Executive Vice-President		
Organisation for Economic Co-operation and Development		
Dirk Pilat, Head		
Canadian Gaming Association	2008/02/07	18
Bill Rutsey, President and Chief Executive Officer		
Robert Scarpelli, Member and Consultant		
Canadian Real Estate Association		
Pierre Beauchamp, Chief Executive Officer		
Gregory Klump, Chief Economist		
Certified General Accountants Association of Canada		
Carole Presseault, Vice-President, Government and Regulatory Affairs		
Genworth Financial Canada		
Francesca Iacurto, Vice-President, Government Relations		
Winsor Macdonell, Vice-President and General Counsel		
Canadian Association of University Teachers	2008/02/12	19
James Turk, Executive Director		
Canadian Chiropractic Association		
Richard Gehrke, President		
John Tucker, Director, Government and Interprofessional Relations		

Organizations and Individuals	Date	Meeting
Canadian Dental Association	2008/02/12	19
Andrew Jones, Director, Corporate and Government Relations		
Darryl Smith, President		
Canadian Healthcare Association		
Denise Desautels, Director, Policy and Communications		
Pamela Fralick, President and Chief Executive Officer		
Réseau des ingénieurs du Québec		
Etienne Couture, President		

APPENDIX B
LIST OF BRIEFS

Organizations and individuals

BIOTECanada

Canadian Advanced Technology Alliance

Canadian Bankers Association

Canadian Chiropractic Association

Canadian Co-operative Association

Canadian Gaming Association

Canadian Healthcare Association

Canadian Medical Association

Canadian Restaurant and Foodservices Association

Canadian Services Coalition

Department of Industry

Design Exchange

Insurance Bureau of Canada

Organisation for Economic Co-operation and Development

Tourism Industry Association of Canada

REQUEST FOR GOVERNMENT RESPONSE

Pursuant to Standing Order 109, the Committee requests that the government table a comprehensive response to this Report.

A copy of the relevant Minutes of Proceedings (Meetings Nos. 4, 5, 7, 8, 10, 11, 13, 14, 16, 17, 18, 19, 23, 26, 30, 32, 34, 36 and 45) is tabled.

Respectfully submitted,

James Rajotte, MP
Chair

Conservative Party of Canada Dissenting Opinion
June 13, 2008

The Conservative Party members put forward the suggestion last fall that the Industry, Science and Technology Committee ("the Committee") undertake a thorough study of Canada's service sector. Throughout the duration of the study members of the Committee heard expert witnesses underscore the strength of Canada's economy, the strength of Canada's services sector and recommendations as to how both Canada's economy and services sector can be enhanced.

At the completion of this study the Conservative members remained steadfast in their conviction that a highly productive services sector is key to the growth of Canada's current and future economy, and acknowledge this crucial sector as a significant provider of highly skilled, high paying jobs.

Furthermore, the Conservative members would like to sincerely thank all of the witnesses for their excellent submissions and testimonies before the Committee. The Committees recommendations were arrived at after thoughtful deliberation. Our members support the majority of the recommendations, but take issue with two put forward by the Committee.

Reinstating GST Rebate for Foreign Visitors:
The Government members do not support the recommendation to reinstate the GST Rebate for Foreign Visitors because the Government has replaced that program with the more effective Foreign Conventions and Tour Incentive Program (FCTIP).

The Government of Canada responded to the needs of the tourism industry in Budget 2007 by creating the new FCTIP. The Visitor Rebate Program was replaced because the program's mandate did not enforce a rigorous standard of accountability of taxpayers' dollars used. Additionally, the program did not effectively increase or enhance Canada as a choice destination as it was designed.

The new FCTIP program is a more effective program than the Visitor Rebate Program at promoting tourism and is a better use of taxpayers' dollars. This new accountable program is aimed at promoting Canada as a choice destination for conferences and tour package travel.

Industry Canada and the Secretary of State for Tourism are in continuous dialogue with tourism stakeholders and the Canadian Revenue Agency to ensure that the implimentation of FCTIP meets the needs of the industry. We are encouraged by the positive feedback of stakeholders thus far.

Additionally, our Government has fulfilled a key campaign promise of reducing the GST from 7 to 5% during our first mandate. Unlike the previous Liberal Government that promised to eliminate the GST but never acted, this Government has delivered on this key campaign commitment. The general reducation to the GST makes Canada's pricing of goods and services more internationally competitive.

Removing the GST on Books:
The Government members strongly support education, educational development, literacy programs and activities, and believe that improving literacy and essential skills are a key part of building Canada's Knowledge Advantage.That said our Members do not support the recommendation of removing the GST on books because exempting specific items from the broad-based goods and services taxes is not good public policy. Rather than exempting specific items from the GST the most effective way to address low literacy is to partner with the provinces and territories and organizations that deliver these literacy activities to create effective literacy programs that help Canadians in their daily lives and in the work place.

While overall Canada has a highly-educated and highly-skilled population, there are still too many Canadians who lack the literacy and essential skills needed for full participation in the workforce and in their daily lives. We can reach many individuals who have low levels of literacy and essential skills through well-designed learning programs that have the workplace as their focus in addition to existing projects focusing on family and community literacy.

Accordingly, the Government of Canada created the Office of Literacy and Essential Skills (OLES) in Spring 2007 to provide a national knowledge base of best practices, models and applied research. As well, the Government created a national knowledge base of practical tools and instruments that support and strengthen partnerships in literacy and essential skills programs that will support efforts to create the best-educated, most skilled and most flexible population in the world.

The Government of Canada is also investing in effective programs that are enhancing Canadians' literacy. Under previous Governments literacy rates among new Canadians decreased. This government is making up for this, by adding $28 million this year for the Enhanced Language Training Initiative, which will help new Canadians join the workforce faster. In addition, we have committed $2.6 billion over 2 years for the Aboriginal elementary and secondary education program. In addition to these programs, we are continuing literacy programs or adding new ones, such as:

- The Adult Learning, Literacy and Essential Skills Program has a budget of $81 million over 2 years.

- Nearly $2.5 million for five different literacy projects across Canada;
- Another $900,000 for the Essential Skills and Workplace Literacy Initiative;
- $73 million over 2 years for the Workplace Skills Initiative;
- $1.6 million for the creation of a National Adult Literacy Database;
- $1.5 million for the Adult Education Skills Development in PEI; and,
- $63 million a year for the Sector Council Program which supports workplace skills and literacy programs in key economic sectors

Furthermore, in a time of limited resources it is important to target literacy assistance to educational institutions because these institutions have the greatest impact assisting Canadians facing literacy challenges. That is why our Government is already providing a GST rebate on books for public libraries, schools, universities, public colleges, municipalities and qualifying charities and non-profit organizations. The cost of the GST rebate on books will be approximately $25 million.

Additionally, the 2% cut to the GST will help all Canadians, specifically lower income families and individuals, to offset the costs of literary and educational goods and services. Unlike the previous Liberal government, when our Conservative government said we would cut the GST we meant it. As promised in our first mandate we have lowered the GST to 5%. This is good news for all Canadians.

Dissenting Opinion
Of the New Democratic Party

To the Standing Committee on Industry, Science and Technology
SERVICE SECTOR REPORT

Respectfully submitted by:
Peggy Nash, MP

Introduction

The Industry Committee has considered the key challenges facing the service sector and worked hard to find agreement on report recommendations. This we were able to do with some proposals, but with others there were strongly divergent views on the issue. Some recommendations would, in our view, take Canada in a fateful direction and do irreversible and unnecessary damage to our country's economy. Hence, the need for this dissenting report.

Economic overview: the Growing Gap

The exuberant description of the Canada's economy in the Committee report is contradicted by many economists and by the lived reality for many Canadians. While some industries have expanded and experienced a labour shortage, others like manufacturing, forestry and tourism are facing serious challenges, especially as key centres and sectors of our economy move into an extended downturn. The most recent labour market reports show unemployment of seven percent or more in seven major urban centres.

The manufacturing sector is in crisis. More than 350,000 good paying jobs have been lost since 2002. The pace of the job loss is actually accelerating with 112,000 of these jobs lost in the year since April 2007. These are for the most part replaced by lower paying service sector jobs and increasingly by self-employment masquerading as job creation.

Most revealing was a recently released Statscan report showing that over the last 25 years in Canada, the gap between rich and poor is widening. While the rich accumulated 16% more wealth, the income of the poorest Canadians declined by 20%. The large group of Canadians in the middle found themselves working longer and harder just to stay in place. [1] Their incomes were stagnant. Meanwhile -personal savings are the lowest in a generation and personal debt is at an all-time high. The Canadian economy may have been growing, but many Canadians were denied the benefits

Canada's Service Sector

Canada's Service Sector is an important part of our changing economy and the Committee's recommendations to promote and support this sector are vital. While some segments such as dentistry and investment banking are characterized by professionals making good salaries, others such as retail, food service, tourism, and personal service are characterized by precarious jobs with low wages and irregular hours. This is a great challenge to those who work in these industries and to the industries themselves.

Some key segments of the service sector are in the public domain. The NDP believes that our social programs and public infrastructure require secure, stable investments to recover from years of neglect. They should not be undermined by corporate tax cuts. We are deeply troubled by tax giveaways that erode our fiscal capacity to properly fund social services and infrastructure.

Tax Strategy:

The NDP accepts as a general principle that personal taxes have to be fair, balanced and progressive. Corporate tax rates should also be balanced, high enough to contribute to the public good, but not be so high as to be an economic disincentive. The report's tax proposal is far too one-sided in favour of across the board tax reductions for individuals and corporations.

Statutory Personal Income Tax

A blanket reduction as proposed by the report would reduce taxes paid by all individuals regardless of income. Therefore rather than targeting aid to low income earners, high income earners with little need for the reduction would also be included and drain significant revenue from the public purse. This would lead to a reduced capacity for government to invest in social programs and benefits that are disproportionately needed by these same low income earners.

Corporate Tax

The Federal Government has already introduced two budgets that have significantly reduced corporate tax rates following on similar cuts by previous governments. This approach with reduce Canada's fiscal capacity by $15 billion a year by 2012 and shifted a greater burden to the individual as personal income tax continues to increase. Billions of these corporate tax reductions went to sectors such and the petroleum and bank industries that are fairly isolated from international pressures and did not require any stimulus. This has left little surplus to bolster sectors such as manufacturing that is experiencing a very serious downturn.

More importantly it has reduced the capacity to invest in our cities and social programs. The Federation of Canadian Municipalities estimates that there is a 60 to 100 billion dollar infrastructure deficit in our country. There are also other financial needs in heath care, housing, education, childcare, and the environment which are all essential to our economic and social prosperity.

As the American economy enters a downturn, economists have predicted a further Canadian slowdown. In this uncertain economic context, coupled with industrial sectors in need of fiscal support and social spending deficits, the report's recommendations on tax reductions cannot be supported.

To encourage the best social and economic environment for the service sector, the government of Canada must stop the parade of tax cuts that are so damaging to the country's fiscal capacity. The government must also end its flirtation with the wholesale privatization of public resources through Public Private Partnerships (P3's); it would only further undermine our fiscal capacity. While some initiatives require the public and private sectors to work together, such as in commercializing new technologies, P3's often leave the public on the hook for future costs while surrendering most benefits to private interests.

Inter-Provincial Trade:

With little study or research, the Committee recommended sweeping support for inter-provincial trade, investment and labour mobility agreements. The NDP appreciates the committee's concern with inter-provincial barriers but we cannot support a policy that would provide unconditional support for the removal of *all* provincial barriers to trade, investment and labour mobility. This is particularly true with regards to the committee's unconditional endorsement of British Columbia and Alberta's Trade, Investment and Labour Mobility Agreement (TILMA).

Governments often place limitations on private investment. In some cases this is done in order to provide designated services of importance. In other circumstances governments use subsidies and procurement policies that support local economic development.

TILMA leaves very little room for public interest policy making of this kind. The agreement creates unparalleled constraints on the provincial governments in question, and does so regardless of whether there is a level playing field for companies in either province.

Agreements like TILMA create excessive pressure to deregulate. The requirement to reconcile regulations and standards is problematic in that the private sector would more often favour and launch complaints over regulations because they are too high – not because they are too low. Equally troubling, sectors such as health and education are not specifically exempted, and this includes agriculture, tourism, parks, heritage conservation, consumer protection, land use planning.

Such broad areas of authority are particularly worrisome as they are coupled with punitive dispute mechanisms that can cause a "chill" effect whereby governments abolish measures or refuse to introduce new ones in fear of TILMA challenges. The NDP cannot support the endorsement of such far-reaching inter-provincial agreements. They pose far too many challenges to the capacity for local governance and public interest decision-making.[2]

Lastly, on the matter of federal leadership in reducing economic barriers between provinces, it appears unrealistic and undesirable for the federal government to assume a leadership role. Any agreements between provinces in this regard would have to be spearheaded and negotiated largely, if not completely by provincial governments and local institutions. The federal government should not take a firm position or leadership role on such matters without a thorough consultation of the provinces.

International Trade

The report asks the government of Canada to build on previous multilateral and bilateral trade deals such as NAFTA. This recommendation is based on the faith that bilateral and multilateral free trade will create sustainable and positive prosperity and employment, despite the facts pointing to greater disparities in wealth and the existence of alternative trade models that differ in both assumptions and solutions.

We remain concerned about the lack of transparency and public discussion about the Canadian government's position in the current Doha talks which include the expansion of the GATS (General Agreement on Trade in Services) with potentially great

consequence for services ranging from post secondary education to energy services, and from health insurance to gambling services.

NAFTA, Bilateral and Multilateral Trade

Recent and long standing reports show that despite being a part of NAFTA, Canada has seen a growing disparity in wealth creation. Those in poverty have slipped further behind, those at the top have continued to climb, and the middle class is barely treading water. Whatever other debates might exist about its impacts, NAFTA has decidedly reduced the policy space available to Canada's governments.

Bilateral deals of the NAFTA type have led to an increase in fiscal, social and environmental dumping, causing downward pressure on taxes, social programs and environmental standards, as investor's demands persistently trump social development, worker's rights and environmental priorities.

Under NAFTA the Government of Canada conceded privileged US access to Canada's strategic oil and gas, water and forests resources, in return for a binding dispute settlement mechanism that failed to work, as evidenced throughout the softwood lumber crisis.

With so many unresolved issues and concerns with the impact of treaties such as NAFTA on areas like our environment and labour standards, future agreements like it should not be blindly endorsed.

Balanced Trade

The NDP believes a Canadian Trade Strategy should be inclusive and not surrender control over key elements of Canada's industrial development and energy policy which ensure that the goals of the market are consistent with the broader public good. A Canadian trade policy must balance the needs of business with those of Canadian citizens and civil society and must be accompanied by flanking policies that ensure public investment in health, education and infrastructure.[3]

Culture and the Arts:

The NDP is pleased that the committee included recommendations that will directly benefit Canada's artists and cultural industry.

New Democrats have called for tax averaging, particularly for artists, for quite some time. Cultural professionals are at a considerable tax disadvantage. Their incomes fluctuate greatly from year to year. In the years they do well, artists pay income tax at a high bracket which means they have little opportunity to save for the very lean times in between. More importantly, this is an issue of tax equity in that many artists can also end up paying more taxes than someone who has earned the same overall income over a set period of years.

We are equally supportive of regulations that would encourage Canadian content and ownership in media. Canada is bombarded on a daily basis by the US, which is the largest and most effective cultural exporter in the world. Canada's cultural workers are at a significant disadvantage in the face of American competition and it is important that

such regulations be adopted in order to protect and further develop a distinct Canadian identity and strong cultural sector.

Canada has many creative industries that are successful here and internationally. However we still too often fail to develop a strategic plan with sound funding and aggressive distribution for much of our culture and too many Canadian artists live in poverty.

Labour Shortage:

Some industry representatives spoke of problems with a labour shortage, particularly in the West. For this reason they argued that it should be easier for seniors to return to the workplace by lowering penalties such as clawbacks on GIS. We are not opposed to seniors working if they so choose. But Canada has built a successful system of pension income for seniors that, if anything, should be improved. Expectations that seniors will return to the workplace can undermine this retirement income system and must be avoided.

It was also suggested by some in industry that the Temporary Workers Program be expanded. Canada needs immigration for continued economic success. Our multicultural society is based on people coming to Canada with the right, not only to work, but also to settle here. People succeed best when they live with their family and in a community. That's why, as well as competing with other countries for skilled immigrants, Canada's family sponsorship program has been a very successful way to help newcomers into Canada. Temporary workers are isolated and are often exploited. This must not be the future path for Canada.

A good way to help address the labour shortage is to provide good family supports such as childcare, flexible hours and benefits to encourage more women into the workforce. Quebec has the strongest provision of family supports and the highest participation of women in the labour market.

Conclusion

Our study of the Service Sector has provided an opportunity to examine the breadth of the service sector and the important contribution it makes to Canada and the world.

It should not be used to overlay a wish list of corporate tax cuts, free trade and cheap labour.

It is an opportunity for Canada to address some of the shortcomings of the Service Sector in a very specific way. We hope that this Committee report and our dissenting report can contribute to the success of Canada's service sector.

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[1] Statistics Canada, "2006 Census: Earnings, income and shelter costs".

[2] Canadian Centre for Policy Alternatives, 'Asking for Trouble: The Trade, Investment and Labour Mobility Agreement', February 2007, from CCPA website: http://www.policyalternatives.ca/documents/BC_Office_Pubs/bc_2007/bc_ab_tilma_summary.pdf

[3] Julian, Peter, Eighth Report of the Standing Committee on International Trade: Dissenting Opinion by the New Democratic Party, March 2007.