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/ THE FEDERAL GOVERNMENT AS AN ENTREPRENEUR,
THE CANADIAN EXPERIENCE /

by

Hugh J. Mullington, B.Comm., D.P.A.

*A thesis submitted to Carleton University
in partial fulfillment of the requirements
for the degree of Master of Arts in Public
Administration.*

School of Public Administration
Carleton University
Ottawa, Canada

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The undersigned hereby recommend to the Faculty
of Graduate Studies acceptance of this thesis,
submitted by HUGH J. MULLINGTON, in partial fulfilment
of the requirements for the degree of Master of Arts.

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THE FEDERAL GOVERNMENT AS AN ENTREPRENEUR,
THE CANADIAN EXPERIENCE

Hugh J. Mullington, B.Comm., D.P.A.

Abstract

Government-owned corporations in Canada appear to be in an evolutionary state. Legislation is expected late in 1969 to create the *Canada Development Corporation* which, as a holding company, is expected to be assigned ownership of *Canadian Overseas Telecommunications Corporation*, *Eldorado Nuclear Ltd.* and *Polymer Corporation*, and which will offer shares to small private investors. Two other corporations, having joint government-private sector ownership - *Telesat Canada Ltd.* and *Panarctic Oils Ltd.* - have also been established in recent months.

This study was undertaken to examine the profitability of existing government-owned companies in the light of the apparently increasing popularity of such entities as instruments of public policy and to consider the task which may face the *Canada Development Corporation* when, and if, it is assigned a supervisory role over several market-oriented crown corporations.

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INTRODUCTION

The thesis which follows analyzes the rationale underlying the creation of proprietary crown corporations by the Government of Canada and compares, where possible, the profit performances of such companies with similar investor-owned corporations in the private sector. In the case of profits realized by crown corporations having no private sector counterparts, the return on the government's investment is compared with average annual yields on long-term federal bond issues.

This study was undertaken to examine the profitability of existing government-owned companies in the light of the apparently increasing popularity of such entities as instruments of public policy and to consider the tasks which may face the *Canada Development Corporation* when, and if, it is assigned a supervisory role over several market-oriented crown corporations.

The use of public corporations by other western democracies is discussed and the importance of government-owned industry to the economies of many nations is noted, illustrating the current diversity of public enterprise. Special attention is drawn to the Italian, Swedish, French, British and American approaches in order to provide a political science framework for the study.

Consideration is given to some of the weaknesses inherent in contemporary Canadian crown corporations in respect to accountability, potential patronage, executive salaries, political interference and pricing policies. The possible future of the government-owned company in Canada is discussed, referring to proposed new crown corporations for the post office and the mint, the *Canada Development Corporation* and to joint government-private sector investment in companies such as *Panarctic Oils Ltd.* and *Telesat Canada Ltd.*

Finally, while recognizing the vital - but often non-compensatory - public service role assigned to many of the present companies, some suggestions are offered for improving the financial performance of crown corporations.

In researching this study, questionnaires were sent to all of the major proprietary crown corporations listed in *Schedule D* of the Financial Administration Act. Heavy reliance was placed on corporate annual reports, extending over many years. Assistance was sought, as well, from commercial attachés at a number of foreign embassies in Ottawa.

The calculations of return on investment used in the analysis in Chapter III are, in every case but one, based on total income (earnings plus interest expense) as a percentage of equity and long term debt, plus major long-term reserves, where applicable. In the case of the one exception - *Farm*

Credit Corporation - for reasons given in the text, calculations for return on investment are based on net income as a percentage of net government investment.

CHAPTER I

GOVERNMENT ENTERPRISE IN WESTERN DEMOCRACIES

The public corporation is an accepted participant in business activity in many western democracies. In Britain, approximately ten percent of the entire labour force is employed in nationalized industry¹; in France, Austria and Italy one-tenth, one-fifth and one-quarter respectively of all industrial output is attributable to state-owned or controlled enterprise².

Many of the world's major industrial firms - 21 of the 200 leading corporations outside of the United States, including the largest companies in France, Mexico, Brazil, Argentina, Austria and India - are government owned*. Other large corporations as, for example, *British Petroleum Ltd.*** - 51 percent controlled by the British Government³ - are at least partially owned by the state.

1. Britain - An Official Handbook - Central Office of Information - London, 1967, P. 251.
2. Rukeyser, William S., Creeping Capitalism in Government Corporations, *Fortune*, Volume LXXVIII, No. 4, Sept. 15, 1968, P. 124.
3. Britain - An Official Handbook - Central Office of Information - London, 1967, P. 252.

* France: Renault - Automobiles, tractors (ranked 16th)
Mexico: Petroleos Mexicanos - Petroleum products (ranked 67th)
Brazil: Petroleo Brasileiro - Petroleum products, synthetic rubber, asphalt (ranked 111th)

Argentina: Yacimientos Brasilero - Petroleum products (ranked 133rd)

Austria: VOEST - Iron and steel (ranked 187th)

India: Hindustan Steel - Iron and steel (ranked 199th)

Source: The 200 Largest Industrial Companies Outside the U.S. - *Fortune*, Vol. LXXVIII, No. 4, Sept. 15, 1968, pages 130 - 136

** Ranked third on *Fortune's* list.

Western governments employ public corporations in manufacturing steel, heavy machinery, munitions, aircraft, automobiles and textiles; to produce lumber, cement, organic and inorganic chemicals, liquors, tobacco products, even bakery goods; to operate railways, airlines, trucking companies, hotels and restaurants. State companies engage in shipping and shipbuilding, mining, banking, communications, broadcasting, printing and publishing. And, through the medium of diversified holding companies, government enterprise extends even further into the fabric of the traditionally private sector of the economy - into construction, catering and merchandising, for example.¹¹

The rationale for public enterprise ranges from doctrinaire socialism, in the case of Britain under the immediate post-war labour government, to the apparently entrepreneurial adventurism found in some Italian government corporations. Objectives vary too, from profit maximization to subsidized social purpose.

West Germany,² for example, generally requires its government corporations to operate profitably. Sweden³ and The Netherlands⁴ expect public companies to recover costs and

1. 1966 Annual Report - Istituto Per La Ricostruzione Industriale, Rome, 1967.
2. Der Bundesminister der Finanzen in letter dated Jan. 23, 1969.
3. The Swedish Budget - A Summary, Ministry of Finance, Stockholm, 1968, P. 48.
4. Mr. J.T.A. Bos, Commercial Attache, Royal Netherlands Embassy, Ottawa, in letter dated December 6, 1968.

show at least some yield on the government capital invested. Japan, on the other hand, looks to its state enterprises to break even.¹ Other countries, notably Britain,² France³ and Italy⁴ are more pragmatic, requiring some companies to attempt to maximize profits while others are justified in terms of public policy.

Italy, with a tradition of government intervention in economic activity that dates back to the 1880's⁵ provides one of the most interesting examples of sophisticated public enterprise at work. Two large government holding companies - *Istituto Per La Ricostruzione Industriale (I.R.I.)* and *Ente Nazionale Idrocarburi (E.N.I.)* have responsibility for all but a very small percentage of the total government investment in industrial and commercial activity. Together these two corporations accounted for almost five percent of the total Italian Gross National Product in 1962.⁶ Both, in fact, are super holding companies, controlling their investments through subsidiary holding companies, with *I.R.I.* operating six⁷ and

1. Mr. Minoru Yoshida, Commercial Counsellor, Embassy of Japan, Ottawa, in letter dated November 29, 1968.
2. Britain - An Official Handbook - Central Office of Information - London, 1967, P. 252.
3. Mr. Jean Trocme, Commercial Counsellor, Embassy of France, in letter dated February 17, 1969.
4. 1966 Annual Report - Istituto Per La Ricostruzione Industriale, Rome, 1967, Pp. 64-66.
5. Posner, M.V. and Woolf, S.J. - Italian Public Enterprise, Duckworth, London, 1967, P. 19.
6. *ibid*, P. 139.
7. *ibid*, P. 43.

E.N.I. three.¹ In many instances, consistent with the practices of conventional holding companies, both *I.R.I.* and *E.N.I.* control their subsidiary firms with but a relatively small minority interest, feasible only because ownership of such companies is shared with many small private shareholders whose holdings are too dispersed to permit effective majority management.

Not all of the subsidiaries, however, involve widely held private shares. A few are wholly-owned by the state holding companies while, frequently, *I.R.I.* or *E.N.I.* participate jointly with other large private sector corporations in the ownership of major industrial firms. Surprisingly, partnership in such joint ventures is not restricted to Italian companies: *U.S. Steel* and *I.R.I.* subsidiary holding companies are joint owners of three large firms - *Deriver*, *C.M.F.* and *Terminos*.² Another important American company - *Raytheon* - owns 45 percent of *Selenia*, matching the extent of an *I.R.I.* subsidiary's holdings.³

Ente Nazionale Idrocarburi, the smaller of the two state holding companies, was created in 1953 to explore, exploit and "engage in development, treatment, transformation, utilization and commerce of hydrocarbons."⁴ Subsequently, the company

1. *ibid*, P. 54.

2. *ibid*, P. 44.

3. *ibid*, P. 44.

4. *Dechert, Charles R.* - *Ente Nazionale Idrocarburi*, *E. J. Brill*, *Leiden*, 1963, P. 4.

extended its interest in the energy field to include nuclear power¹ and later ventured into other sectors, into publishing and manufacturing of machinery, controls, textiles and textile products.² Its activities in petroleum exploration and refinery operations extend to several foreign countries, including Germany, Switzerland, Egypt, Iran, Libya, Tanganyika, Tunisia, Morocco, Nigeria and Ghana. In 1961 the estimated value of E.N.I.'s assets ranged from 760.4 billion lire (approximately \$1.225 billion) to 1,240 billion lire (approximately \$2.0 billion.)³

Extensive as they may be, E.N.I.'s and its subsidiaries' holdings are eclipsed by those of its giant sister corporation, *Istituto Per La Ricostruzione Industriale* in both value and scope. I.R.I. was formed twenty years earlier than its younger counterpart, in 1933, and - in terms of assets - is more than twice the size of E.N.I.⁴

At the end of the 1967 fiscal year, including its five principal holding companies, I.R.I. had 65 direct subsidiaries; another 86 companies are either wholly owned or controlled by the subsidiary holding companies.⁵ Among these are such internationally known companies as *Alitalia*, the state

1. *ibid*, P. 6.

2. *ibid*, P. 6.

3. *ibid*, P. 95 (See also Posner and Woolf, Page 155) Regretably, no later statement of the value of E.N.I.'s assets could be obtained.

4. Posner, M.V. and Woolf, S.J. - Italian Public Enterprise, Duckworth, London, 1967, P. 56.

5. 1967 Annual Report - Istituto Per La Ricostruzione Industriale, Rome, 1968, Appendix V - Organization Chart (See also Rukeyser - Creeping Capitalism in Government Corporations, Fortune, Vol. LXXVIII, No. 4, Sept. 15, 1968, P. 143)

airline, (91.2 percent owned by I.R.I.) and *Alfa Romeo*, world-renowned for its high performance automobiles (49.0 percent owned by I.R.I.)¹ The Company's holdings encompass three of the largest banks in Italy - *Banca Commerciale Italiana* (95.5 percent I.R.I. ownership), *Credito Italiano* (81.4 percent ownership) and *Banca di Roma* (96.0 percent ownership) as well as several other major Italian financial institutions.² I.R.I. also either owns or controls large engineering, steel, ship-building and electrical companies having dominant roles in their respective industries.³ In the service sector, the holding company enjoys a near-monopoly in radio and television broadcasting, telecommunications, telephone and airline operations while also prominent in water and road transportation. In addition, small subsidiaries are active in the operation of construction, merchandising, hotel, restaurant and catering companies, among others.

As the end of 1967, I.R.I.'s total assets amounted to 6,298 billion lire, or approximately \$10.2 billion.⁴

The diversity of I.R.I.'s and E.N.I's activities is perhaps best explained by Posner and Woolf's observation that, although the minister of state holdings is held responsible to

1. *ibid*, Appendix III.

2. *ibid*, Appendix III.

3. Posner, M.V. and Woolf, S.J. - *Italian Public Enterprise*, Duckworth, London, 1967, Pp. 43-52.

4. *1967 Annual Report*, Istituto Per La Ricostruzione Industriale, Rome, 1968, P. 88.

parliament for the corporation's actions:

In practice ... I.R.I. and E.N.I. decide themselves on the size and composition of their investment programmes, and are swayed only marginally by ministerial - still less parliamentary - opinion. Where the institute itself is uncertain about a course of action, the minister's voice may be decisive. Thus, on the Taranto steel works, Finsider and the I.R.I. Institute tended at one stage to take divergent views, and governmental voices had the casting vote. Again, when the investment programmes were being assessed in crisis conditions in 1963, ministerial support doubtless reinforced the cautious optimism of the Institute's own plans. But on the whole we suggest the usual conclusion: he who pays the piper calls the tune. It is only the power over the purse strings - so complete in the U.K., so slight in Italy¹ - that enables Government views to prevail.

While the Italian case appears to be an extreme example, holding companies are not unusual in state enterprise. Spain's *Instituto Nacional de Industria* has been recognized as a replica of I.R.I. in both objectives and operating methods.² Austria too has made a recent step in the direction pioneered by I.R.I. in establishing a holding company known as *Oesterreichische Industriewerwaltung GmbH (O.I.G.)*, in 1967, to supervise the operations of 21 government corporations. The companies which fall under the aegis of O.I.G. dominate Austria's metals industries and have importance in chemicals, oil and machinery.³

1. Posner, M.V. and Woolf, S.J., Italian Public Enterprise, Duckworth, London, 1967, P. 39.
2. Rukeyser, William S., Creeping Capitalism in Government Corporations, *Fortune*, Vol. LXXVIII, No. 4, Sept. 15, 1968, P. 193.
3. *ibid.*, P. 193.

Britain has grouped a number of public companies engaged primarily in road transportation and a travel agency, *Thomas Cook & Son*, under the *Transport Holding Company*¹ and is reported to be in the process of considering creation of a new corporation - presumably also a holding company - to supervise the activities of all nationalized industry in the United Kingdom.² Another holding company, *Industrial Reorganization Corporation*, was established in Britain as recently as 1966 to participate in the concentration, rationalization and modernization of industry, promoting mergers and regrouping of firms to take advantage of economies of scale.³ The objectives of this latter company would appear to be much more orientated towards implementation of government policy than towards commercial success in terms of its own corporate profits. In this respect, however, it is not alone.

Both Britain and France provide particularly interesting examples of state enterprise being charged with socio-political objectives. The French tobacco and match monopoly, *Service d'Exploitation Industrielle des Tabacs et des Allumettes (SEITA)*, whose origins date back to the

1. *Britain - An Official Handbook - Central Office of Information, London, 1967, Pp. 251, 346, 353, and 354.*
2. *Rukeyser, William S., Creeping Capitalism in Government Corporations, Fortune, Vol. LXXVIII, No. 4, Sept. 15, 1968, P. 193.*
3. *Britain - An Official Handbook - Central Office of Information, London, 1967, P. 252.*

Napoleonic era, is required to recruit veterans, persons physically handicapped by war injuries, widows and orphans of individuals killed in war.¹ Similarly, Britain's *Remploy Ltd.*, a non-profit public company operates factories giving employment to severely disabled people who are unlikely to obtain work except under special conditions.²

There are other likenesses between Britain and France in their approaches to the use of government corporations. One writer has noted, for example, in referring to nationalization of industry which took place in both countries following the end of the Second World War, that:

*The post-war nationalizations of Great Britain and France and the Soviet organization of state industries are probably the only examples of the creation of a series of public corporations based on definite political and legal theory.*³

and

*The series of nationalization laws which, after the last world war socialized, in Britain, the basic industries of coal, transport, electricity and gas, and, in France, coal, electricity, gas and press enterprises, were the expression of a political philosophy which demanded the public control of these as well as certain other enterprises.*⁴

Both countries have established public corporations to operate

1. *Le Secretaire General, Service d'Exploitation Industrielle des Tabacs et des Allumettes*, in letter dated March 20, 1969.
2. *Britain - An Official Handbook*, Central Office of Information, London, 1967, Pp. 252 and 430.
3. *Friedmann, W. - The Public Corporation - A Comparative Symposium*, Carswell & Co., Toronto, 1954, P. 542.
4. *ibid*, P. 544.

state airlines, railways and coal mines; both have created government-owned radio and television broadcasting corporations and both entrust operation of electrical power generation facilities to state enterprise. The two countries differ somewhat, however, in their respective attitudes towards responsibility to parliament for the performance of government corporations.

Friedmann notes that the British legislation "shows the most serious attempt to blend autonomy and public responsibility"¹ and points out that "ministers will not normally answer questions in parliament relating to day-to-day management and the current conduct of business operations."² An official British government publication supports Friedmann's assessment with the following statement:

The public corporation today is, generally speaking, a public body having a clearly defined and specific task. Its managing board and its staff are chosen for their experience and competence in a particular field; they are not civil servants, and although they are accountable to Parliament in a variety of ways, it is they and not the ministers of the sponsoring departments who are responsible for the management of the corporations.

By contrast, French ministers are held responsible to parliament for public corporations under their jurisdiction and may be interrogated regarding the activities of state companies. Moreover, the minister can also be required to submit reports on corporations for which he is responsible. As a result, many

1. *ibid*, P. 580.

2. *ibid*, P. 581.

3. *Britain - An Official Handbook*, Central Office of Information, London, 1967, P. 251.

decisions require prior ministerial approval.¹ In addition, corporations are subject to close scrutiny from the Investments Commission of the Ministry of Finance and Economic Affairs, and from subcommissions established in both the Assembly and the Senate.²

Still another approach to the use of public corporations is found in Sweden where the government has established three classes of such instruments: public enterprises, government-owned business companies, ~~ex~~cluding credit institutes, and credit institutes.

Public enterprises are defined as:

...government agencies, not independent legal entities though their freedom in economic and staff matters is greater than that of other government agencies. They are expected to cover operating costs (including depreciation) from their current receipts, besides showing some yield on the government capital invested in them. Thus, they are not expected to maximize profits.

Such agencies include the Board of Telecommunications, which operates the national telephone network and provides transmission facilities for radio and television; the State Railways which, in addition to railway service, where an almost complete monopoly prevails, also engage - through subsidiaries - in the operation of bus lines, ferries and road transport companies; the State

1. Hanson, A.H. (ed.) - Public Enterprise - International Institute of Administrative Sciences, Brussels, 1955, P. 209.
2. *ibid*, P. 210.
3. The Swedish Budget, 1968-69, Ministry of Finance, Stockholm, 1968, P. 48.

Power Board, which provides 43 percent of all electric power produced in Sweden;¹ ~~the State Forest Service~~ which administers the government's forests and certain agricultural properties; the *National Defence Industries*; the *Airport Administration Board* and the *Post Office*.

The public enterprises have no independent borrowing powers and must rely on the central government for all long-term capital. Even depreciation funds must be returned to the government which can then vote investment capital through the budget. All surpluses, which amount to net profit plus interest on capital borrowings, must be paid over to the government. Understandably, in the light of the foregoing, public enterprises in Sweden do not pay central government taxes.

Government-owned business companies are described as:

*.... independent legal entities (whose) activities are subject to the regulations in the Companies Act. Government influence is exerted via shareholders' meetings, which also determine the dividends. Profits after dividends are ploughed back into the company in question.*²

It should be noted that the expression "government-owned" referred to above does not necessarily imply 100 percent ownership. In fact, varying degrees of private participation are found in several of these entities, including the state monopoly - *Vin & Spritcentralen Ltd.* - which engages in

1. *ibid*, P. 49.

2. *ibid*, P. 49.

importing, producing and wholesaling of wines, liquors and strong beers. In this case non-governmental holdings amount to less than three percent of total invested capital but private shareholdings amount to as much as 50 percent in the case of some "government owned companies".

Also included in this category of Swedish public corporations are ~~monopolies~~ monopolies for retailing alcoholic beverages, the operation of football pools and the management of monthly money lotteries. The largest government-owned company, aside from the monopolies, is *LKAB* - 95.7 percent owned by the government - which mines iron ore deposits in the north of Sweden. Wholly-owned government companies include: *North Bothnian Steelworks Ltd.*; *Statsgruvor Ltd.*, which mines iron, lead and zinc; *National Forest Industries Ltd. (ASSI)*, which produces sawn timber and wallboard, pulp and kraft liner and manufactures paper sacks in a recently-purchased factory in the United Kingdom; *Svenska Skifferoljeaktiebolaget Ltd.*, a holding company controlling porous concrete fabricators and manufacturers of mineral wool and steel shot, and *Swedish Map and Printing Organization Ltd.* which prints and publishes maps.

Public companies having non-governmental shareholdings are: *Aerotransport Ltd.*, holding company for Sweden's share of *Scandinavian Air Systems (SAS)*, 50 percent owned by the government; *Swedish Atomic Energy Co. Ltd.*, 57 percent

government-owned; *Karlskrona Shipyards Ltd.*, which engages in engineering and shipbuilding, 95.7 percent owned by the state; *Uddevalla Shipyards Ltd.* 50 percent owned; *Central Restaurant Co. of Sweden Ltd.*, which provides hotel and catering services, and *Swedish Tobacco Co. Ltd.*, manufacturers and sales agency for tobacco products, both 99 percent owned by the government.

Credit institutes are also share companies but, unlike other government companies, their activities are governed by the Bank Act. At present there are two established companies in this field - the *Swedish Credit Bank Ltd.* and the *Postal Bank*. A third, the *Investment Bank of Sweden*, was created in 1967 and is still in an evolutionary form.

Although Friedmann claims that Sweden has "contributed little to the theory and practice of public corporations"¹ and Hanson argues that Sweden "... is not a country famous for its public enterprises,"² there can be little doubt that the Swedish approach to control of public corporations, as exercised through restrictions on investments, in the case of "public enterprises", and through shareholders' meetings, in the case of government-owned companies, is worthy of attention. Also, Sweden's cooperation with neighbouring Norway and Denmark, in the ownership of *Scandinavian Air Systems*, offers a rare

1. *Friedmann, W. (ed.) - The Public Corporation, A Comparative Symposium*, Carswell, Toronto, 1954, P. 546.
2. *Hanson, A.H. (ed.) - Public Enterprise - International Institute of Administrative Sciences*, Brussels, 1955, P. 182.

example of joint international public ownership. Significantly, too, *Aerotransport Ltd.* - Sweden's holding company for its 3/7 share of *SAS* is itself only 50 percent state-owned. Cooperation with the private sector, though also found in Italy, and, to a lesser extent in Britain, is another area in which Sweden has contributed to the theory and practice of public corporations, providing guidance for Canada and other countries presently experimenting with such an approach.

The critical quotations referred to above might have been more accurately directed towards the United States, which - perhaps because of the influence of Republican governments and the strong free enterprise sentiment which prevails in the U.S. - has employed public corporations infrequently. Yet, even in this case, the example of the *Tennessee Valley Authority (TVA)* is worthy of note.

Friedmann has pointed out that:

*.... at least outside the United States, the Tennessee Valley Authority has been accepted as an outstanding example of successful public enterprise in a definitely non-socialist country.*¹

and he adds, quoting Professor Albert S. Abel:

.... it is clear that for some reason or another, the region where it (TVA) operates has advanced industrially and economically relatively faster than the country as a whole.

Despite the success of the *TVA*, the United States has made relatively little use of the public corporations, except

1. Friedmann, W. (ed.) - *The Public Corporation - A Comparative Symposium*, Carswell, Toronto, 1954, P. 546.
2. *ibid*, P. 546.

during wartime. A number of writers, including Friedmann and Hanson, have expressed the view that public corporations in the United States have often been faced with hostile legislation. Another author quotes a resolution adopted some years ago by the United States Chamber of Commerce which urged that "no more government corporations be created and that existing corporations be liquidated as soon as possible." He adds that this "was by no means an isolated viewpoint."¹

Abel, in his analysis of the public corporation in the United States, concluded:

*Primarily, however, the public corporation has been avoided unless its margin of efficiency in the three areas mentioned (personnel, budgeting and auditing requirements) would make an appreciable contribution to the achievement of the programme to be administered.*²

Accordingly, the United States has generally tended to limit its interest in public companies to special types of insurance and credit agencies such as the *Export-Import Bank*, the *Commodity Credit Corporation*, *Federal Crop Insurance Corporation*, *Federal Deposit Insurance Corporation* and the *Federal Savings and Loan Insurance Corporation*. Corporate form, however, has been used for the operation of the two U.S. international canal ventures - the *Panama Canal Company* and the *Saint Lawrence Seaway Development Corporation*, as well as the *TVA*.

1. Seidman, H. - The Government Corporation: its Place in the Federal Structure, included in Hanson, A.H. (ed.) - Public Enterprise - International Institute of Administrative Sciences, Brussels, 1955, P. 41.
2. Abel, Albert S. - The Public Corporation in the United States, included in Friedmann (ed.) The Public Corporation, Cresswell, 1954, P. 356.

Of these, only the *TVA* can be considered comparable to typical public corporations found in most western democracies. Other American government corporations have more closely resembled agencies or departments of government since the passage of two acts - the *Ramspeck Act* and the *Government Corporation Control Act* - in the 1940's.

The *Ramspeck Act*, at the option of the President, provided for the extension of civil service laws to employees of federally-owned and controlled corporations. The *Government Corporation Control Act* imposed government budgetary and auditing requirements on U.S. public corporations. Significantly, the *TVA* was specifically exempted from the *Ramspeck Act* provisions and was "singled out for exemption in some aspects of the auditing requirements" laid down in the *Government Corporation Control Act*.¹ The fact that no other U.S. public company fared as well was not viewed with concern by some observers. An officer of the U.S. Bureau of the Budget, supporting the curtailment of public corporations noted:

*From the very beginning it was inevitable that the corporation, if it were to survive as a government institution, would have to be assimilated into the government structure. Under our system of government no public institution, corporate or non-corporate, can be permitted for long to act contrary to the policies and wishes of those who bear political responsibility for the actions of the government. Separations of management and ownership may have occurred in private industry but such a development cannot be permitted in government if we are to preserve our democratic institutions.*²

1. *ibid*, P. 357.

2. Seidman, H. - *The Government Corporation: Its Place in the Federal Structure*, included in Hanson, A.H. (ed.) - *Public Enterprise*, International Institute of Administrative Services, Brussels, 1955, P. 48.

Abel and others, however, have taken a somewhat different position, claiming that the two acts have gone far "toward completing the task of eliminating the features which made government corporations useful instruments for enterprise purposes."¹

The American experience has not been duplicated in Canada.

1. Abel, Albert S., - The Public Corporation in the United States - included in Friedmann, W. (ed.) - The Public Corporation, Carswell, Toronto, 1954, P. 357.

CHAPTER II

CANADIAN CROWN CORPORATIONS - THEIR ORIGINS AND DEVELOPMENT

The origins of Canadian government companies, or crown corporations as they are officially designated, predate Confederation. Hodgetts has noted that the earliest crown corporation on record was the *Board of Works* formed by Lord Sydenham to construct a canal system for the United Provinces which between 1841, when it was established, and 1846 when it became a department of government, enjoyed corporate status.¹ The government-financed *Nova Scotia Railway Company* was in operation as early as 1859² and Ashley and Smails have pointed out that a number of harbour boards were established as crown corporations before Confederation.³

Provincial and municipal crown corporations appeared early in the Twentieth Century, the *Hydro-Electric Power Commission of Ontario* having been created in 1907.⁴ The first significant federal crown company appeared following the incorporation of *Canadian National Railways*, in 1919.⁵

It was not until the mid-1930's, however, that the Canadian government "displayed any marked inclination to

1. Hodgetts, J.E. - Proceedings of Fifth Annual Conference of Institute of Public Administration of Canada, P. 389.
2. Stevens, G.R. - Canadian National Railways, Clarke, Irwin, Toronto, 1962, Vol. 1, P. 163.
3. Ashley, C.A. and Smails, R.G.H. - Canadian Crown Corporations, MacMillan, Toronto, 1965, P. 5.
4. Hodgetts, J.E. - The Public Corporation in Canada - included in Friedmann, W. (ed.) - The Public Corporation, A Comparative Symposium, Carswell, Toronto, 1954, P. 51.
5. ibid, P. 57.

experiment extensively with the device of the public corporation."¹ Hodgetts attributes the change in the government's attitude to the depression, the criticism of private enterprise expressed by the socialist Cooperative Commonwealth Federation (CCF), the experiments with the New Deal in the United States and the growing recognition of the use of public enterprise in the United Kingdom.²²

In the 1930's corporate status was extended to the *Canadian Wheat Board* (1935), the *Canadian Broadcasting Corporation* (1936), *Trans-Canada Airlines* (1937) and the *Bank of Canada* (1938). Later, during World War II, a number of wartime crown corporations were established, primarily because the Liberal government of Mackenzie King and, especially, the then Minister of Munitions and Supply, C. D. Howe, regarded the crown corporation approach as the most expeditious means of producing war materials. A few of these have survived, notably *Polymer Corporation* (1942), *Eldorado Nuclear Ltd.* (1944) and *Canadian Arsenal Ltd.* (1945).

Other crown corporations, unrelated to the war effort, came into existence during the mid-1940's and the early post-war period. Included amongst these were the *Industrial Development Bank* (1944), *Exports Credit Insurance Corporation* (1944), *Central Mortgage and Housing Corporation* (1945) and *Northern Transportation Co. Ltd.* (1947).

1. *ibid*, P. 52.

2. *ibid*, P. 52.

These were followed by such companies as *Crown Assets Disposal Corporation* (1950), *Canadian Overseas Telecommunications Corporation* (1950), *Defence Construction Ltd.* (1951), *Atomic Energy of Canada Ltd.* (1952), *St. Lawrence Seaway Authority* (1952), *Eldorado Aviation Ltd.* (1953), *Farm Credit Corporation* (1959) and *Seaway International Bridge Corporation* (1963).

Canadian Crown corporations now manufacture munitions, chemicals and synthetic rubber; mine and refine uranium; engage in lending activities for residential construction, agricultural or industrial purposes; insure mortgages and exports; operate railways, trucking companies, hotels and restaurants, airlines, ports and harbour installations, water transportation entities, an international inland waterway, tolls bridges and telecommunications facilities; market grains, nuclear reactors and surplus government assets; manage radio and television broadcasting networks; offer international transportation consulting services; generate hydro-electric power and provide central banking services.

Subsidiaries of Canadian crown corporations - either wholly or partly-owned - can be found in several foreign countries, including the United States, Britain, France, Switzerland, Italy, the Netherlands, Belgium, Mexico and Jamaica.

Moreover, there are indications that further additions will be made to the ranks of Canadian government corporations

in the near future. Most prominent among these proposed new creations is the *Canada Development Corporation*, first announced in the Speech from the Throne following the election of the Liberal government in 1963.¹ Two existing entities, the post office and the mint,* currently organized along departmental lines, are also reported to be in the process of conversion into crown corporations.^{2,3} And legislation for the establishment of a government-controlled satellite communications company, *Telesat Canada*, recently received parliamentary approval.⁴

Although, at first glance, it might appear that most - if not all - functions performed by crown corporations could be carried out by private industry, ideology has not played a role in the emergence of public enterprise in Canada. It is, in fact, ironic that the only Canadian political party to have openly favoured government enterprise - the CCF-NDP - has never held federal office. By contrast, the two major parties, the Liberals and Conservatives, have both created crown corporations - without ideological commitment. The Liberals, particularly if wartime instrumentalities are

1. *Canada, House of Commons Debates*, 1963, P. 7.
 2. *How Post Office Will Plan for a Profit - Just Like a Business* - *Financial Post*, December 28, 1968.
 3. *Mint Will Become Crown Corporation* - *Globe and Mail*, Feb. 18, 1969.
 4. *Canada's Satellite Up In '71*, *Ottawa Journal*, June 14, 1969.
- * At time of writing, this matter was under discussion. Subsequently, on May 27, 1969, Parliamentary approval was given to an act establishing the Royal Canadian Mint as a Schedule C, or Agency corporation.

included, have begotten the great majority of crown corporations. On the other hand, the Conservative Party, while "critical of this form of organization and equivocal in its attitude"¹ formed the government which passed the original legislation creating four of the most important crown corporations: *Canadian National Railways, Canadian Wheat Board, Bank of Canada and Canadian Broadcasting Corporation.*

It is apparent, in the absence of ideological stimuli, that pragmatism has played a dominant role in the Canadian approach to public enterprise. Musolf has observed, in his study of public ownership in Canada, that:

*The government, for its part, has not exhibited - under either the Conservatives or the Liberals - any inclination to push public enterprise for its own sake; in this it has but mirrored its recognition and approval of private enterprise as the foundation of the economy. Although it has not shrunk from taking action necessary to attain the goal of economic unity, even if this has meant launching a commercial venture, it has done so only in response to demonstrated need.*²

Hodgetts has reached much the same conclusion in his analysis of the subject, noting that "It cannot be said that any unifying philosophy underlies the use of the public corporation in Canada: the whole development has been piece-meal and pragmatic."³

1. Ashley, C.A. & Smalls, R.G.H. - Canadian Crown Corporations, Macmillan, Toronto, 1965, P. 6.
2. Musolf, Lloyd D., - Public Ownership and Accountability, Harvard, Cambridge, 1959, P. 11.
3. Hodgetts, J.E. - The Public Corporation in Canada, included in Friedmann, W. (ed.) The Public Corporation, A Comparative Symposium, Carswell, Toronto, 1954, P. 53.

The Honourable C. D. Howe who, as wartime minister of Munitions and Supply, presided over the creation of some 28 crown corporations established for war purposes, revealed the criterion he adhered to in respect to the use of crown corporations when he stated:

*If private business was able to carry out the war objective, private business was given that opportunity. The government has created crown companies only to undertake work that private industry was not willing to undertake.*¹

Earlier, in a more generic discussion, he had stressed:

*....there is only one test of the strength and weakness of either private operation or government operation, namely, which can best serve the needs of the people of Canada.*²

Prime Minister Louis St. Laurent echoed this sentiment in the post-war period when he asserted his view:

*I think we are all most happy when free enterprise does what is required to be done and public authorities do not have to intervene.*³

In fact, governmental intervention in business through nationalization is rare in Canada. Among existing proprietary crown corporations only two - *Canadian National Railways* and *Eldorado Nuclear Ltd.* - owe their origins to nationalization. A third crown corporation, *Canadian Overseas Telecommunications Corporation*, acquired the facilities of two private companies engaged in external telecommunications by expropriation in order to meet the requirements of an agreement concluded among Commonwealth countries.

1. *Canada, House of Commons Debates*, 1946, P. 2176.

2. *ibid*, 1945, P. 1397.

3. *ibid*, 1952, P. 4764.

In the case of *Canadian National Railways*, nationalization was necessitated to ensure the continued operation of a series of insolvent railroad lines. On the other hand, *Eldorado's* take-over was carried out for strategic reasons - to ensure Canada and her allies of a dependable source of high grade uranium for military requirements.

Polymer Corporation, though differing from *Eldorado* insofar as it was not originally established by private capital, also emerged out of strategic necessity - to provide an alternate source of rubber to meet wartime demand.

By and large, however, Canadian crown corporations have been created to serve the cause of national unity and to promote economic development. *Canadian National Railways*, in particular, emerged from the consolidation of several insolvent railroad ventures to provide vital regional and transcontinental rail service, linking areas not covered by the *CPR*. *Air Canada* was incorporated, for similar reasons, because private capital would not undertake the risk involved. The *Farm Credit Corporation*, *Exports Credit Insurance Corporation*, and *Central Mortgage and Housing Corporation* all have national economic significance, the latter having universal application while the two former agencies are confined to particular sectors of the economy. The *St. Lawrence Seaway Authority* and *Canadian Overseas Telecommunications Corporation* have been created to build, operate and maintain important national assets. The

Canadian Broadcasting Corporation was established to foster "national consciousness" and strengthen "national unity".¹

Although Canadian governments have shown a distinct preference for the use of crown corporations when commercial or quasi-commercial objectives have been involved, spokesmen for both major parties have been somewhat inconsistent in their attitude, appearing to suggest, especially when in opposition, that corporate status was not a particularly desirable alternative to departmental organization. A Conservative Member of Parliament, for example, could say:

*The official opposition does not believe in crown corporations. We think that it is one method of getting away from control by Parliament.*²

The fact that the Conservatives, when restored to power a few years later, created the *Canadian World Exhibition Corporation* (1962) did not dissuade another Conservative from subsequently arguing, after his return to opposition ranks:

*Surely the time has come when we should return parliamentary powers to Parliament. Let us stop appointing Royal Commissions and creating crown corporations to denude Parliament of its powers.*³

Mackenzie King, showing the frustrations of a member of the opposition, when restricted in obtaining information on the operation of *Canadian National Railways*, reacted in similar vein, contending:

1. *ibid*, 1932, Pp. 3035-36 (R.B. Bennett)
2. *ibid*, 1949, P. 1035.
3. *ibid*, 1965, P. 354.

....it should be a matter of principle that there is nothing connected with the properties that the people of Canada own that the people's representatives in this Parliament should not have a right to inquire into, not at one particular time, but at all times the vaster the organization, the greater the need for publicity.¹

King rather nimbly embarked on a different tack, however, as Prime Minister, defending the independence of the CNR with the following words:

But while he is president of the Canadian National, and we are representing the people of Canada in this House, we propose to give Sir Henry Thornton the same degree of latitude and freedom as the shareholders of the Canadian Pacific would give to Mr. Beatty.²

The crown corporation form of organization has found other advocates, among members of both parties, when sitting on the government side of the House. Arthur Meighen, an early defender, in arguing the case for *Canadian National Railways* being a crown corporation before his brief term as Conservative prime minister, noted:

Now, while it is conceivable that the Inter-colonial Railway - as a partially business concern, but having other and bigger purposes - may have been best managed by a department of the government in the early years of this country's history, it is utterly inconceivable that a tremendous aggregation of railways, a great system such as the Canadian National system has now grown to be, could ever be conducted along that line....³

C. D. Howe, Liberal "Minister of Everything" in the King and St. Laurent cabinets, explaining the government's use

1. *ibid*, 1920, P. 1669-ff.
2. *ibid*, 1923, P. 3673-ff.
3. *ibid*, 1920, Pp. 1664-66.

of crown companies during wartime, identified the advantages of using corporate organization:

The corporation is an accepted unit of Canadian business. Corporate practice is well understood by those engaged in private business. The corporate system of accounting is also well understood and has been highly perfected through experience over the years. Therefore, to bring into being a form of organization which was readily understood, to make it sufficiently flexible so that the head office could be established in a location most convenient to those men whom we wished to attract to the business, and to secure other advantages which appealed to us at the time, were the determining factors which led us to carry out a number of war operations through the agency of crown corporations.¹

Howe's personal bias in favour of corporate organization was clearly revealed in his reply to a question in the House regarding the need for extending corporate status to the Dominion Coal Board:

All I can say is that for a commission to operate and do business it seems necessary that they be formed into a corporation. All the commissions I know of that operate around Ottawa are formed into corporations I do not know why, other than that a corporation is a convenient form. It provides convenience of accounting and an accepted pattern of doing business that is lacking when three men simply form themselves into a committee.²

Not surprisingly, in light of the views of Mr. Howe and others, crown corporations already account for a substantial percentage of Canadian federal public service employment. As of March 31, 1968, the work forces of these companies, including instrumentalities such as the Bank of Canada, the Canadian

1. *ibid*, 1946, P. 1512.

2. *ibid*, 1947, P. 4249.

Wheat Board, Canada Council, etc., amounted to more than 137,000, or approximately 35 percent of all federal government civilian employment.¹ A change in the present status of the post office and the mint, if staff strengths remain constant, would raise total crown corporation employment to approximate parity with that of all remaining government departments combined.

In the case of the post office and the mint, the motivation for converting these agencies to crown corporation status is, apparently, the desire to have them perform on a compensatory basis. This has not been true of all existing crown corporations. Many have objectives which are essentially regulatory or administrative in nature and are therefore dependent upon government grants or appropriations. Several have service roles which are essentially non-commercial and, consequently, also depend on appropriations. Only relatively few have clearly recognizable commercial responsibilities and, even among these, self-sufficiency is not a common characteristic.

The *Financial Administration Act* was enacted by Parliament in 1952 to provide, among other purposes, for the identification and classification of crown corporations, grouping them essentially according to their objectives. The act thus recognizes three generic types of crown corporations: *Schedule B*, or Departmental Corporations; *Schedule C*, or Agency

1. Report of the Auditor General to the House of Commons, Queen's Printer, Ottawa, 1968, Pp. 284-286.

Corporations, and *Schedule D*, Proprietary Corporations. A number of crown corporations, nonetheless, still fall outside of the Act and are commonly recognized as "Unclassified Crown Corporations". Among these are the *Bank of Canada*, the *Industrial Development Bank*, the *Canada Council* and the *Canadian Wheat Board*.

The *Financial Administration Act* defines *Schedule B* corporations as those that act as "servant or agent of Her Majesty in right of Canada and (are) responsible for administrative, supervisory or regulatory services of a governmental nature". *Schedule C* corporations are described as those acting as "an agent of Her Majesty in right of Canada and (are) responsible for the management of trading or service operations on a quasi-commercial basis, or for the management of procurement, construction or disposal activities on behalf of Her Majesty in right of Canada". A *Schedule D* corporation is defined as one which:

- " i) is responsible for the management of lending for financial operations, or for the management of commercial and industrial operations involving the production of or dealing in goods and the supplying of services to the public, and
- ii) is ordinarily required to conduct its operations without appropriations."¹

It is this latter group which most closely resembles corporations in the private sector and which, in some cases,

1. *Financial Administration Act*, R.S.C. 1952, C. 116 as amended April 1, 1969, Part VIII, section 76(3).

compete - to varying degrees - with private companies. As such they are not always held in high esteem by businessmen who argue that they provide competition which is subsidized and therefore unfair.

The late R. A. Emerson, then president of *Canadian Pacific*, expressed a view held by many business leaders in a speech delivered at the 1965 annual meeting of the *Canadian Manufacturers Association* when he stated that crown corporations had incurred losses totalling \$619 million during the previous five years, and continued:

These losses must be financed through taxation and, to a very significant degree, through corporate income tax

*... In this way serious competitive disabilities are created for business firms which, to survive, must earn taxable income and thus incur tax liability.*¹

Another criticism has been expressed, in comments invited by the writer, by the president of *Pacific Western Airlines*, Mr. R. H. Laidman, who noted:

It has often been calculated by the experts that the monopoly held by Air Canada retarded total air transportation in Canada, something in the order of perhaps ten years. There is now some hopeful possibility of a break-through in this area and while it does not too directly affect this company, some of Air Canada's present social routes could be served by regional carriers who would require some subsidization but substantially less drain on the public purse than the internal cross subsidization carried out by Air Canada (about \$18,000,000 annually).

The area in which the Air Canada monopoly has most seriously affected Pacific Western has been in its ability to impede the transcontinental growth of

1. CPR Heads Rap Crown Firms over Competitive Policies, *Financial Post*, June 12, 1965, P. 18.

*C.P. Air. Without increased growth trans-continentially, C.P. Air was not in a position to divest itself of any regional routes in British Columbia. Obviously, the effect on us was just as serious but it was indirect.*¹

These are, unquestionably, strong criticisms. Both imply that crown corporations, if severed from government subsidy support and forced to face competition in the marketplace, would not likely survive. Yet to what extent is this assumption justified? Some proprietary crown corporations are - or have been - profitable even while fulfilling public service responsibilities. Others were never intended to do more than "break even". Still others, also *Schedule D* Corporations, were always recognized to be very largely dependent upon appropriations or subsidies.

The diversity of proprietary crown corporations makes it impossible to generalize in respect to *Schedule D* companies. The fact, however, that they do resemble private companies in their organization and accounting practices invites some comparisons with private enterprise.

1. Laidman, R.H., in letter to the author, March 10, 1969.

CHAPTER III

FINANCIAL PERFORMANCES OF PROPRIETARY CROWN CORPORATIONS

There is no doubt that a number of *Schedule D* crown corporations are - in the commercial sense of the word - unprofitable. Indeed, several fail to meet one of the prime qualifications established in the *Financial Administration Act* differentiating between proprietary crown corporations and departmental and agency companies, i.e., ".... ordinarily required to conduct (their) operations without appropriations."¹ In examining proprietary crown corporations it is necessary to recognize that, ignoring supporting subsidiaries, *Schedule D* firms fall within two distinct categories: those whose operations are compensatory, showing some return on invested capital, and those whose revenues are insufficient to meet their financial obligations, making them dependent upon subsidies of various types

These compensatory and non-compensatory groupings have been sub-divided, for the purposes of this analysis, into corporations which are comparable to private sector firms and those which are not. Hence, the twelve* *Schedule D* crown

1. *Financial Administration Act*, R.S.C. 1952, C. 116 As amended April 1, 1969, Part VIII, Section 76(3)ii.

* Although the present roster of *Schedule D* crown corporations totals 15, three have not been included in this study. They are: Cape Breton Development Corporation, whose objectives are of a socio-political nature with regional impact; Eldorado Aviation and Seaway International Bridge Corporation, both of which are essentially supporting subsidiaries of other proprietary crown corporations.

corporations that will be considered from the viewpoint of financial performance can be grouped as follows:

GROUP I - Compensatory Corporations

(i) Comparable to the private sector:

*Air Canada
Eldorado Nuclear Ltd.
Polymer Corporation*

(ii) Not comparable:

*Canada Deposit Insurance Corporation
Canadian Overseas Telecommunications Corporation
Central Mortgage & Housing Corporation
Exports Credits Insurance Corporation
Northern Transportation Company Ltd.*

GROUP II - Non-compensatory Corporations

(i) Comparable to the private sector:

Canadian National Railways

(ii) Not comparable:

*Canadian Broadcasting Corporation
Farm Credit Corporation
St. Lawrence Seaway Authority*

While it is clear, as Hodgetts has noted, "... that the reasons which induced private entrepreneurs to employ the corporate form are not relevant for the state as entrepreneur",¹ there is no reason to accept the view that public enterprise should not be expected to produce a return on invested capital. As noted earlier, West Germany, Sweden and the Netherlands expect that public corporations in their respective countries should earn at least some return on government capital invested.* In this same context, joint public-private sector

1. Hodgetts, J.E. - The Public Corporation in Canada, in Friedmann, W. (ed.) The Public Corporation, Carswell, Toronto, 1954, P. 60.

* See Chapter I.

ownership of subsidiaries of state holding companies, as found in Sweden and Italy, necessitate a profitable performance if only to ensure that private shareholders receive a yield on their investment in the corporation. In fact, if government companies do not at least break even in their operations, the short-fall constitutes a direct subsidy to the users of the services provided by the corporation, at the expense of the public purse. Indeed, it should be recognized that the difference between the actual financial performance of a public corporation and an accepted private sector return on an equivalent amount of invested capital is the true measure of the subsidy involved.

This should be particularly so of proprietary crown companies with the possible exception of the *Canadian Broadcasting Corporation*, whose services are almost universally available to all Canadians and whose deficits must be financed out of annual parliamentary votes. At least in this case, the public and its representatives in Parliament can be made aware of the actual cost of this service and have the opportunity to express its will in respect to the continuance of financial support for the national broadcasting network.

It is interesting to note that all of the proprietary crown corporations in groups I or II above enjoy either oligopolistic or monopolistic positions in domestic markets. Yet, many of these firms are constrained in pricing their

services or products, either by foreign competition, market conditions or public policy considerations. *Air Canada*, for example, acts in concert with other airlines in establishing prices for international traffic, particularly on overseas routes. *Polymer* and *Eldorado* are dependent upon foreign demand for much of their production. And *Farm Credit Corporation* was obliged by Act of Parliament, until November 1968, to charge no more than 5% on loans to farmers.¹ Similar circumstances prevailed, though to a much lesser degree, in respect to *Central Mortgage and Housing Corporation* as well until the free-floating mortgage rate was adopted by the government in early 1969.

Nonetheless, Group I crown corporations have generally produced profits on a fairly regular basis. Three of these firms - *Air Canada*, *Eldorado* and *Polymer* - bear some resemblance to private sector companies and, to some extent, comparisons may be drawn between public and private enterprise in these cases. Other corporations in this group either fulfill special governmental functions or, as in the case of *Northern Transportation*, are so unique as to have no private sector counterparts.

In order to assess the profitability of these proprietary crown corporations, earnings - over a minimum of five years - have been examined to determine the annual return

1. Report of the Auditor General to the House of Commons, 1968, Queen's Printer, Ottawa, Pp. 203-204.

on invested government capital. And, in the case of those corporations which are similar to private sector companies, specific comparisons - to the degree that such is possible - are offered.

ANALYSIS OF GROUP I
PROPRIETARY CROWN CORPORATIONS

Compensatory Corporations
Comparable to the Private Sector

AIR CANADA

The *Air Canada* annual report for 1968 contains return on investment data for the period 1959-68 inclusive. The company, consistent with the practices of other North American airlines, uses the United States' *Civil Aeronautics Board* formula to derive this particular statistic. Under the CAB method, net income (after income tax), plus interest expense, is expressed as a percentage of average investment which is recognized as the sum of long term debt and shareholders' equity.¹

The Corporation's return on investment performance for the years 1959-68 inclusive and relevant financial data is present in Table 1.

1. *Air Canada, 1968 Annual Report, P. 21*

TABLE 1 - AIR CANADA - FINANCIAL PERFORMANCE 1959-68

<u>YEAR</u>	<u>NET INCOME AFTER TAXES</u>	<u>INTEREST EXPENSE</u>	<u>LONG TERM DEBT</u>	<u>SHAREHOLDERS' EQUITY</u>	<u>RETURN ON INVESTMENT</u>
	(ooo)	(ooo)	(ooo)	(ooo)	%
1968	8,184	18,247	392,820	24,614	6.3
1967	3,547	13,857	302,820	16,630	5.2
1966	2,910	11,580	235,820	13,283	5.4
1965	3,990	11,298	235,820	10,573	6.1
1964	1,406	11,491	235,820	6,783	5.2
1963	528	11,619	237,471	5,528	4.8
1962	(3,541)	11,519	237,471	5,000	3.1
1961	(6,450)	10,511	227,671	5,000	1.5
1960	(2,607)	8,097	209,100	5,000	1.8
1959	153	3,731	135,100	11,842	2.7

Source: Air Canada, 1968 Annual Report, Pp. 22-23.

Air Canada's return on investment, in 1968, compared favourably with American Airlines (6.7%), TWA (6.1%), United Airlines (6.0%) and Eastern Airlines (2.0%), while lagging significantly behind Delta (15.8%), Northwest Orient (15.4%), Braniff (7.8%), Western Airlines (7.7%) and Pan American World Airways (7.6%).¹ The average, however, for all United States' airlines in 1968 was 7.1%,² still considerably above the Air Canada return, which was the company's highest in the past decade.

Comparisons available for previous years indicate that considerable volatility exists in respect to the profitability

1. Air Carrier Financial Statistics, United States' Civil Aeronautics Board, Washington, 1969, P. 35.
2. Air Canada Results Nearing U.S. Levels, Financial Post, April 12, 1969.

of airlines in the United States: by contrast, *Air Canada's* performance has been relatively stable during the past five years. It is clear, however, that *Air Canada* is among the least profitable of the major North American airlines.

TABLE 2 - COMPARISONS - RATES OF RETURN ON INVESTMENT -
AIR CANADA AND MAJOR U.S. AIRLINES*

YEAR	AIR CANADA		EASTERN		UNITED		DELTA		WESTERN	
	AMERICAN		TWA		BRANIFF		NORTHWEST		PAN AMERICAN	
(percentages)										
1968	6.3	6.7	2.0	6.1	6.0	7.8	15.8	15.4	7.7	7.6
1967	5.2	8.8	8.2	8.0	10.4	5.8	19.8	20.2	11.7	10.5
1966	5.4	10.5	6.5	8.9	7.2	12.6	25.8	20.6	15.9	14.2
1965	6.1	10.1	12.6	13.8	9.7	13.6	21.6	24.0	15.2	12.4
1964	5.2	9.7	1.8	13.2	7.5	10.2	16.6	19.3	19.0	11.3
1963	4.8	7.2	(-12.2)	10.9	5.3	3.9	12.2	10.8	15.2	11.7
1962	3.1	5.4	(-2.0)	3.4	4.2	5.5	15.0	8.1	10.4	6.9
1961	1.5	4.2	(-1.4)	(-6.1)	3.1	4.3	8.0	5.9	4.0	4.9

Sources: *Air Canada Annual Report, 1968*; *U.S. Civil Aeronautics Board, Handbook of Airline Statistics, 1967 edition, P. 384*; *Air Carrier Financial Statistics, 1969, P. 35.*

Another yardstick that can be applied to measure the performance of *Air Canada* is to compare the company's yield on

* Comparison data for Canadian Pacific Airlines and Pacific Western Airlines were not available, except for the years 1966 and 1967. In those years, return on investment results for the two carriers, ranked second and third in Canada, were as follows:

	CPA	PWA
1967	13.7%	2.7%
1966	30.5	8.6

It should be noted that, because much of CPA's flying equipment is leased from CPR, it is impossible to derive a valid comparison for return on investment with *Air Canada* and other airlines. Moreover, CPA regards its return on investment data as confidential, having advised the writer to this effect in correspondence dated March 7, 1969. (CPA and PWA statistics derived from the airlines' annual reports.)

invested capital with interest levels in corresponding periods. The company's 1968 return was more than one half of one percent lower than the prime commercial lending rate for chartered banks, and, even more significant, also fell below the yield on Federal Government bonds having durations of 10 or more years. This is not unusual for *Air Canada*, as is shown in Table 3.

TABLE 3 - AIR CANADA - COMPARISON OF RETURNS ON INVESTMENT WITH INTEREST LEVELS

<u>YEAR</u>	<u>AIR CANADA RETURN ON INVESTMENT</u>	<u>AVERAGE CHARTERED BANK - COMMERCIAL PRIME LENDING RATE</u>	<u>AVERAGE FEDERAL GOVERNMENT BOND YIELDS 10 YEARS & OVER</u>
	%	%	%
1968	6.3	6.91	6.73
1967	5.2	5.91	5.94
1966	5.4	6.00	5.44
1965	6.1	5.75	5.22
1964	5.2	5.75	5.18
1963	4.8	5.75	5.08
1962	3.1	5.75	5.11
1961	1.5	5.63	5.04
1960	1.8	5.75	5.18
1959	2.7	5.14	5.07

Sources: *Air Canada*, *Bank of Canada*.

During the past year, *Air Canada* increased its long term debt by \$90 million.¹ The company has indicated that it will need a further \$300 million over the next five years

1. *Air Canada*, 1968 Annual Report, P. 4.

and \$820 million in the next decade, to finance new equipment and property.¹ Since 1965 *Air Canada* and other crown corporations' borrowings from the Federal Government have been assessed interest charges amounting to 1/8 of one percent above the rate paid by the government itself. Currently, that rate is 7½ percent.² New loans and maturing issues that have to be re-financed must bear the higher rate of interest, reducing the company's net income accordingly. Hence, a considerable improvement in *Air Canada*'s profitability is required if the company is to meet its obligations "without appropriations".

Moreover, the company may not be able to depend on its traditional sources of capital loans - *Canadian National Railways* and the Government of Canada - for further large-scale borrowings. There have been several indications that *Air Canada* might be encouraged, by the government, to enter the bond market - or even offer shares publicly - in order to raise its own capital. In his November, 1967, budget speech the then Minister of Finance, Mitchell Sharp, commented:

*Another demand upon our funds is Air Canada. It is having to expand rapidly its fleet of aircraft and its various ground installations in order to meet the growing traffic demands on it. The Minister of Transport and I recognize that it will be necessary to exercise restraint on what the government lends to Air Canada in future years, requiring that company to seek sources of capital funds other than the government.*³

1. Pratte, Yves, (Chairman of *Air Canada*) in speeches to *Canadian Club of Toronto*, January 27, 1969, and *Canadian Society of New York*, March 7, 1969.
2. Dr. A.G. Irvine, Director, *Crown Corporations Financing*, Department of Finance, Ottawa, Interview August 26, 1969.
3. House of Commons Debates, 1967, P. 4904.

The availability of relatively low-cost capital has been highly advantageous to the company in the past. Had *Air Canada* previously been faced with interest costs associated with open-market borrowings, its next earnings would undoubtedly have been significantly below the levels attained in recent years. Conversely, unless a substantial improvement in the company's income is achieved in the near future, *Air Canada* may have little appeal, as a shareholding investment, to the general public. In such a situation the bond market would be a logical source of funds. In this case, however, a sizeable annual debt service obligation, at significantly higher than present rates of interest, would also be incurred.

Nevertheless, *Air Canada* may have obtained at least a temporary respite from the new policy implied in Mr. Sharp's remarks. Although there have been no official disclosures on the subject, the company is reported to have been assured that it will be able to continue, in the short term, to depend on Federal Government loans. The Financial Post, early in 1969, carried the following account:

....Neither *Air Canada* nor government officials are prepared to comment on the situation. But it appears the reasoning to stay out of the market is basically two-fold:

- The state of the bond market, and present rates being demanded, makes it unattractive if the step can be avoided.
- A bond issue would require a prospectus giving the airline's plans, which at this time nobody could seriously draft or guarantee. Until the

cabinet has completed its study of the corporate direction to be taken by Air Canada, any long-run predictions are of dubious value.

This, coupled with Ottawa's desire to trim its (U.S. currency) reserves has been enough to dictate the present policy.¹

Though the pressure may now have been lifted in respect to a demand for "outside" financing, Air Canada is still faced with a need to enhance its earnings, if only to afford the new aircraft already on order. While the company expects to almost double its passenger volume - from 6.5 million in 1968, to approximately 12.0 million by 1973² - it is placing heavy reliance on such new equipment as the jumbo jets, the Lockheed L-1011 and the Boeing 747, and - in the longer term - on the supersonic Concorde and Boeing 2707. The company's record of success with new aircraft, however, has not been outstanding, as noted by one leading transportation economist:

Between 1955-60 Air Canada doubled its size in terms of available aircraft ton-miles, but unit costs per ton-mile fell by only 3%. The introduction of Viscounts and Super Constellations had little impact on unit costs.³

Pan American Airways has been quoted as expecting a similar

1. *Baxter, Clive: Air Canada Plans No Trip to Bond Market, Financial Post, February 15, 1969.*
2. *Pratte, Yves, Chairman, Air Canada, in speech to Canadian Society of New York, March 7, 1969.*
3. *Hogg, Vincent (Chief Transportation Economist, World Bank), Speech: The Economics of Changing Transport Technology, McGill University Symposium, Montreal, May 29, 1969.*

reduction in moving from Boeing 707's to 747's.¹ But critics have pointed out that public reaction to these new aircraft is unknown. Some suggest that the public will not readily be induced to use the jumbo jets unless substantial savings - as yet unproven - are available. Also it may be too much to expect would-be passengers to pay the premium rate that, apparently, will be required to fly on supersonic aircraft for savings of two or three hours on a trans-Atlantic crossing. On the other hand, the supersonic equipment should have substantially greater potential annual revenue miles than conventional sub-sonic jets, giving rise to more efficient utilization of capital. And, if the potential of jumbo jets is developed, the expectations of *Air Canada* and other airlines for large increases in revenue passengers may be borne out.

There is some evidence that the company's management has begun to take steps, in addition to new aircraft acquisitions, which may result in improved profits. The new chairman of the airline, Yves Pratte, has emphasized this approach in several speeches:

....On the open market, we won't be able to fall back exclusively on our crown corporation status when justifying our profit position.

Let me assure you that we're not going to get caught short. Whether necessary or not, we intend to measure up to whatever profit standards the investment community applies to private airlines; and we intend to do it without ceasing to discharge our obligations as a national carrier.²

1. *ibid.*

2. Pratte, Yves, in speech to Canadian Society of New York, March 7, 1969.

More recently, the Minister of Transport, the Honourable Don C. Jamieson, through whom the corporation reports to Parliament, departed from a prepared speech to reveal that the government plans to make *Air Canada* "... responsible to the demands and pressures of the market place," adding, "Because it is publicly owned it ought not to escape the tests of efficiency and good financial management that can be applied to private ventures."¹

This new attitude represents a considerable departure from the "public service" concept which prevailed in 1937 when the airline was first established. A statement made by C. D. Howe during the debate on the incorporation of *Trans-Canada Airlines*, *Air Canada's* predecessor, illustrates the prevailing policy of the government at that time:

*The set up is such that the company will be protected against loss, but its profits will be very strictly limited. In other words, it is organized to perform a certain national service, and it is expected that that service will be performed at or near cost.*²

And *Air Canada's* ex-President, Gordon McGregor, has made it clear that Howe wanted primarily to avoid losses, having told McGregor "You stay out of the taxpayers' pockets and I'll stay out of your hair."³

1. Jamieson, Don C., Minister of Transport, in speech at Canadian Aviation Industry Dinner, Vancouver, August 7, 1969, Remarks carried in Canadian Press Dispatch, Ottawa Journal, August 8, 1969.
2. Canada, House of Commons Debates, 1937, Pp. 2042-43.
3. MacSween, Joseph, McGregor - Life Always Up in the Air, Ottawa Journal, July 12, 1969.

However, *Air Canada*, as conceived by Howe, was, as Pratte has noted, "...never intended to be a large international profit-making organization."¹ Yet, the company has become an important international carrier - the eighth largest in the world, in 1968, and the largest outside the United States and the U.S.S.R.² As such it is imperative that, if Canadians are to avoid subsidizing passengers of other nationalities using the airline, *Air Canada's* net income should be at least as great as the rate of interest applicable to its new borrowings, and preferably high enough to provide some additional return to the Federal treasury, commensurate with the risks involved in airline investment.

ELDORADO NUCLEAR LTD.

In 1968 *Eldorado* reported net income of \$178,860, representing a return on invested capital of less than one-half of one percent. Similar results were obtained in both 1966 and 1967, reflecting the depressed world market demand for uranium. In the same period, however, the two other major Canadian uranium producers - *Denison Mines Ltd.* and *Rio Algom Mines Ltd.* - both registered substantial profits. Comparisons of the financial results of the three companies are given in Table 4 below.

1. Pratte, Yves, in speech to Canadian Society of New York, March 7, 1969.
2. *ibid.*

TABLE 4 - FINANCIAL COMPARISONS - ELDORADO NUCLEAR LTD.,
DENISON MINES LTD. AND RIO ALGOM MINES LTD.

YEAR	ELDORADO		DENISON		RIO ALGOM	
	INVESTMENT (ooo)	RETURN %	INVESTMENT (ooo)	RETURN %	INVESTMENT (ooo)	RETURN %
1968	\$ 52,211	0.3	\$ 82,469	15.5	\$ 199,365	6.5
1967	52,032	0.5	74,607	11.4	193,846	5.8
1966	51,763	0.3	69,401	10.2	159,925	5.8
1965	52,587	2.7	67,625	14.8	157,322	5.2
1964	52,001	4.8	62,290	9.0	164,292	4.7
1963	51,051	5.5	60,429	15.6	163,036	6.3
1962	50,268	8.5	66,696	15.3	104,266	7.9
1961	49,058	4.4	62,973	22.4	94,105	13.6
1960	51,845	6.7	65,491	23.1	96,688	6.4
1959	53,306	7.8	46,291	38.7	N.A.	N.A.

Sources: Annual Reports, Eldorado, Denison & Rio
Algom (for data on income and investment;
calculations for return by the author)

While Eldorado's profit performance over the past five years has dwindled to nearly zero, it would be unfair to carry the comparison with the results achieved by Denison Mines Ltd. and Rio Algom Mines Ltd. too far. Although all three companies had, as their primary purpose, the mining and milling of radioactive ores, both Denison and Rio Algom used earnings from uranium sales to expand and diversify their holdings, branching out into other mining ventures and into industrial interests. The growth of Denison's investment - almost all generated from retained earnings - and its extremely attractive yield over the past six years testified to the success of that

company's efforts to protect itself from the anticipated decline in demand for uranium. Similarly, *Rio Algom* has been able to increase its total investment through a successful common stock issue, while maintaining a relatively stable return on capital, despite a severe reduction in the demand for its major product.

Denison, for its part, used retained earnings from its substantial profits in the peak years of uranium production to acquire controlling interest in *Lake Ontario Cement, Canada Cement, Concord Finance*, eleven different mining corporations, three concrete products companies and a real estate holding company, while also establishing an oil and gas division. *Rio Algom*, on the other hand, used both profits and new capital raised from sales of common stock to gain entry into steel and titanium milling, metals distribution and base metal mining, investing as well in such developments as the Churchill Falls power project. Both companies thus insulated themselves against the eventual loss of markets for uranium and, as a result, have continued to produce good returns on their respective investments. *Eldorado*, by contrast, has been almost entirely dependent upon uranium for its income and has therefore suffered a sharp decline in its profitability.

It would be a mistake, however, to suggest that *Eldorado's* management lacked the foresight, imagination and aggressiveness necessary to take action similar to that taken by *Denison* and *Rio Algom*.

The management of the company has, since its inception as a proprietary crown corporation, apparently been guided by both profit objectives and public policy considerations. The original order-in-council authorizing the creation of *Eldorado* in 1944, clearly expressed the view that the company should operate profitably:

*.... having regard to the fact that the main business of the corporation consists of the exploration, development and operation of mineral properties and the production, refining and sale or disposal of radium and other products, it is desirable and in the public interest that the said business should be carried on as nearly as possible in the same manner as the business of an ordinary trading or commercial company with share capital.*¹

In 1948, at the request of the Federal Government, *Eldorado* - in addition to its mining and refining operations - began to act as the official purchasing agency for all uranium produced in Canada. Subsequently, between 1953 and 1957, the company entered into a series of contracts with private producers in Canada to purchase uranium and negotiated agreements with foreign buyers for the sale of the product. This role, understandably, was carried out at cost, as a public service to the uranium industry.

Eldorado's profits, however, from the operation of its uranium mines were substantial. The original government

1. *Special Committee on Research, Minutes of Proceedings and Evidence No. 1, 1960-61, Statement by Mr. W.M. Gilchrist, president, Eldorado Mining & Refining Ltd. (Now Eldorado Nuclear), P. 12.*

investment in the company, at the time of its expropriation, amounted to \$5,271,812, payable to the former shareholders, and a further \$3,975,065 subscribed for new shares. In 1949, the company redeemed one million dollars worth of capital stock, reducing the government's investment to a total of \$8,246,877. By the end of 1959 the company had paid dividends of \$19,740,000,¹ and had accumulated cash reserves, from earned surpluses, totalling \$13,200,000. The return on government capital invested in the first 15 years of the company's operations thus totalled \$32,940,000, equivalent to an average yield on capital of better than 10 percent per annum.

During this period of high profits, the management of *Eldorado* recognized that an over-supply situation was developing in the industry and sought to discover non-nuclear uses of uranium which would stimulate demand. In 1956 a research and development division was established, while joint studies were continued, in cooperation with metallurgical research personnel of the *Department of Mines and Technical Surveys*. However, research was not viewed as the only solution for *Eldorado*. The following passage, quoted from minutes of the *House of Commons Special Committee on Research* in 1961, illustrates both the approach taken by the company and the subsequent problems which resulted:

1. *ibid*, P. 43.

The Chairman: You mentioned this morning that you have ceased your activities as a crown corporation in exploration.

Mr. Gilchrist (President of Eldorado): Yes.

The Chairman: Would you mind explaining to the committee about this decision.

Mr. Gilchrist: ...Eldorado was in the business of prospecting and exploring for uranium as early as 1944 to 1946, because at that time they knew that the demand was going to increase. Then they made attempts to find or encourage, or to bring in private operators

We continued that phase of our activity until early in 1956 when the general supplies of uranium became more than were required....

However, two years later, in 1958, it became quite clear that our mine in the Northwest Territories, at Great Bear Lake, was going to run out of ore, that the ore body would be exhausted likely sometime in 1960. This proved to be the case.

That operation ceased in September 1960, but it was the only commercial activity on Great Bear Lake and in that part of the Northwest Territories. We had the necessary transportation system developed, and well-developed, and the mine provided an excellent basis for exploration in the immediate vicinity.

When I say "immediate vicinity" I mean within a radius of anywhere from zero to 100 miles. We thought it was a shame to walk away without making an effort to use this base to develop the area somewhat further. In other words, even if we pick up a base metal ore body. So we took the matter to our minister and suggested that we go back into the exploration field in that particular area, not on a national or countrywide basis, but to see if we could perpetuate the activity and keep something moving in that area. Mr. Churchill* agreed, and we organized it on a five year basis We went forward on that basis.

Our first year in the field was 1959 and the following year, 1960, just past We had developed a few promising mineralized zones zones that indicated that further work should be done. However, there was strong opposition developed from the mining industry at large to a crown company being in

* Minister of Trade & Commerce

the exploration business. As has been stated here, the Canadian Metal Mining Association indicated their wish to put in a brief and to make representations to this committee in regard to this matter. I understand also that the prospectors' organization and the B.C. Chamber of Mines were going to make representations to the government or to this committee.

So, in view of the opposition and the criticism that was developing it was decided that Eldorado should retire from the exploration business..... We are doing so at the minister's request, or the committee of the cabinet on matters of uranium.¹

Mr. Forgie: When was the decision made to retire from the field of active exploration?

Mr. Gilchrist: This was within about the last month.

Mr. Gilchrist, referring to the order-in-council establishing Eldorado (see page 49), went on to add:

A mining company of our size and stature would have an exploration arm, in the normal course of events, and the directors and myself strongly recommended to the government that we get into this, because we have taken a good many millions of dollars out of the Great Bear area, and this was one way of putting some of it back into it. In other words, we took the attitude that you are either in the mining business, or you are out of it. It was our feeling that we should be in it in all phases or that we should be out of it.²

It was also pointed out that no private interests were working in the area at the time that Eldorado embarked on its exploration program.

It is clear, from the foregoing, that Eldorado's management took steps to improve the company's future earnings prospects, in the face of expected curtailment of sales of its primary product. However, as a public enterprise, the company

1. *ibid*, Pp. 179-180, underscoring mine.

2. *ibid*, P. 180, underscoring mine.

was restrained by the government since policy considerations dictated avoidance of further governmental competition with the private sector.* The decline in *Eldorado's* earnings which resulted, and the accompanying decrease in government income from this source should, therefore, be attributed to the government itself and not to the management of the crown corporation.

It is difficult not to conclude that Mr. Gilchrist's argument that *Eldorado* should be in "all phases" of the mining business or "out of it" is sound. *Eldorado* can hardly be expected to show a respectable return on the government capital invested if the company's management is not permitted to take entrepreneurial action when such is necessary.

The following disclosure - which appeared in the crown corporation's 1968 annual report - would seem to indicate that this fact has now been recognized by the government and that the company will no longer be hampered in this respect:

*The restriction on outside exploration, which has been imposed upon the company by government policy for some years was lifted in mid-1968. As a consequence, activities have been extended to areas remote from the Beaverlodge complex and plans for a number of projects are underway.*¹

1. *Eldorado Nuclear Ltd., 1968 Annual Report, P. 8.*

* *Eldorado was, in effect, already in competition with private uranium producers insofar as the companies all operated in a limited market, with the result that private operators were deprived of the opportunity of selling the uranium that Eldorado itself supplied to foreign buyers.*

POLYMER CORPORATION

Like *Eldorado*, *Polymer Corporation*'s origins as a government enterprise date back to World War II. The Japanese conquests in Asia, which resulted in the capture of most of the world's natural rubber resources, made it necessary for the Allied Powers to turn to the production of synthetic rubber in order to meet the demands of the war effort. The Canadian approach to this problem was to establish *Polymer* as a crown corporation in 1942, and entrust it with the construction and management of a government-owned plant, at Sarnia, Ontario, for manufacturing synthetic rubber from petroleum gases.

In this case, there was no doubt of the government's intent with respect to the post-war operation of the plant, at least in the mind of C.D. Howe who stated, in the House of Commons, in 1943, that:

*It is the intention of the government to continue to operate the plant at Sarnia to make rubber for the country at war and the country at peace.*¹

Ashley & Smails suggest also that Howe expected *Polymer* to be operated as though it were a privately-owned company, the board of directors of which would be judged by its ability to

1. House of Commons Debates, 1943, P. 3707, quoted in Ashley, C.A. & Smails, R.G.H., Canadian Crown Corporations, Macmillan, Toronto, 1965, P. 229.

show a profit in the face of competition once the supply of natural rubber was restored.¹

Until 1951, *Polymer* operated the plant, providing what amounted to managerial services, under the terms of an agreement between the corporation and the government, which retained title to all assets. As a result, profits arising from the venture were not subject to corporate income tax. During this period the company's annual returns on the government capital invested in plant and facilities were as follows:²

1944	--	1948	(-0.6)%
1945	--	1949	1.5%
1946	6.1%	1950	1.7%
1947	8.4%	1951	9.4%

Viewed in the context of the corporate tax exemption that *Polymer* enjoyed during its first nine years of operation, the company's profits were, at best, nominal during this time.

However, in April 1951, the government sold the plant and other assets to *Polymer* for their depreciated value, becoming both shareholder and debenture-holder in the process. As a result, the corporation's management assumed responsibility for operating in accordance with accepted commercial procedures and *Polymer* lost its tax exempt status.

1. *Ashley, C.A. & Smalls, R.G.H., Canadian Crown Corporations, Macmillan, Toronto, 1965, Pp. 228-229.*
2. *ibid*, P. 237.

The profitability of the company, already showing some improvement in the year immediately preceding the reorganization, increased substantially. With government approval, *Polymer* acted aggressively to develop export markets for its excess domestic production - an essential step for a company with a plant capacity, at that time, of 50,000 tons of synthetic rubber annually when its Canadian market did not exceed 20,000 tons.¹ Subsequently, foreign subsidiaries were established in Switzerland, The Netherlands, Belgium, France, Italy, Mexico and South Africa; other foreign offices are maintained in both England and the United States. The company also secured government authorization to diversify its production and to market by-products of its synthetic rubber output. The results of these developments are reflected in the company's record of profits dating from its acquisition of the government's assets which are detailed in Table 5 (page 57).

While *Polymer* enjoys a monopoly position within Canada in the manufacture of synthetic rubber it does meet competition from two major chemical companies - *Dow Chemical of Canada Ltd.* and *Monsanto Canada Ltd.* - in respect to its plastics production. Unfortunately, neither of these firms separate their Canadian financial results from those of their American parent corporations, with the result that relevant data required for comparisons were not obtainable. However, inasmuch as *Polymer*

1. *Canada, House of Commons, Minutes of Committee on Public Accounts, 1961, especially P. 323.*

can be regarded as essentially a chemicals producer, in the generic sense, some comparisons can be derived for three non-competing Canadian chemicals companies. These are presented in Table 6 (page 58).

TABLE 5 - POLYMER CORPORATION, FINANCIAL PERFORMANCE,
1952-68 INCLUSIVE

<u>YEAR</u>	<u>NET PLANT VALUE</u>	<u>TOTAL INVESTMENT</u>	<u>NET PROFITS</u>	<u>RETURN ON INVESTMENT</u>	<u>DIVIDENDS</u>
	\$ (ooo)	\$ (ooo)	\$ (ooo)	%	\$ (ooo)
1968	83,965	155,437	7,038	4.5	3,000
1967	86,821	152,886	5,821	3.8	3,000
1966	75,421	130,073	11,221	8.6	4,500
1965	60,163	121,261	10,303	8.5	4,500
1964	61,870	116,021	9,450	8.1	4,000
1963	65,686	104,359	9,138	8.8	3,250
1962	55,023	90,655	10,284	11.3	3,000
1961	36,456	73,734	10,220	13.9	3,000
1960	31,389	64,670	9,851	15.2	3,000
1959	31,976	57,750	3,690	6.4	3,000
1958	34,502	57,060	6,377	11.2	4,000
1957	34,036	54,683	6,823	12.5	4,000
1956	32,598	51,860	9,450	18.2	6,000
1955	30,592	48,409	7,531	15.6	5,000
1954	30,583	45,878	4,925	10.7	3,000
1953	32,818	46,953	5,098	10.9	3,000
1952*	34,911	47,855	2,798	7.8	2,500

Sources: Polymer Corporation, Annual Reports,
1952-68.

* 1952 results based on nine month period from
March 31, 1952, to December 31, 1952, only.

TABLE 6 - COMPARATIVE RETURN ON INVESTMENT PERFORMANCE -
POLYMER CORPORATION AND CANADIAN INDUSTRIES
LTD. (CIL), DUPONT OF CANADA LTD., AND UNION
CARBIDE OF CANADA LTD., 1958-67 INCLUSIVE.*

<u>YEAR</u>	<u>POLYMER</u>	<u>CIL</u>	<u>DUPONT</u>	<u>UNION CARBIDE</u>
	%	%	%	%
1967	3.8	3.3	6.9	6.5
1966	8.6	7.9	9.6	9.1
1965	8.5	5.1	8.8	9.9
1964	8.1	5.8	18.2	9.7
1963	8.8	5.8	15.8	7.8
1962	11.3	4.7	15.1	N.A.**
1961	13.9	4.1	N.A.	N.A.
1960	15.2	5.1	N.A.	N.A.
1959	6.4	4.8	N.A.	N.A.
1958	11.2	4.0	N.A.	N.A.

* 1968 annual reports for CIL, Dupont and Union Carbide were not available at time of writing.

** Annual reports were not available for these years.

Sources: Polymer Corporation, Canadian Industries Ltd., Dupont of Canada Ltd. and Union Carbide of Canada annual reports.

While the above comparisons have only limited validity, it is evident that *Polymer's* performance relates very well to those of both *CIL* and *Union Carbide*, though falling well behind that of *Dupont of Canada*. A more realistic indication of *Polymer's* performance might be obtained by analyzing the company's profitability in relation to other synthetic rubber producers, particularly those in the United States and Western Europe. Such data, however, were not available to the author.

One other crude indication of the relative profitability of the company can be derived from reference to industrial medians published for American industry. This, of course, is especially

imperfect in respect to *Polymer* since the company can, in fact, be classified as either a rubber producer or a chemicals manufacturer. As a result, reference is made to both industries, in Table 7, in an attempt to establish a range of profitability which might be applicable to United States producers of synthetic rubber.

TABLE 7 - RETURN ON INVESTMENT COMPARISONS - POLYMER CORPORATION AND UNITED STATES INDUSTRIAL MEDIANS FOR CHEMICALS AND RUBBER INDUSTRIES, 1966-68 INCLUSIVE

<u>YEAR</u>	<u>POLYMER</u>	<u>CHEMICALS INDUSTRY</u>	<u>RUBBER INDUSTRY</u>
	%	%	%
1968	4.5	9.7	11.3
1967	3.8	10.0	9.1
1966	8.6	12.6	11.2

Sources: Polymer Corporation Annual Reports, Fortune, Vol. LXXIX, No. 6, May 15, 1969, and Fortune, Vol. LXXVII, No. 7, June 15, 1968. Data prior to 1966 for industrial medians are not available.

Unfortunately, similar statistics for Canada, on an industrial basis - which would be more pertinent to *Polymer* - are only now becoming available and are even more limited in duration than the American data cited in Table 7. The *Dominion Bureau of Statistics* began, in 1969, to publish information on financial characteristics of Canadian companies, using an industry-by-industry format. To date, however, only one report, for the year 1966, has been produced.¹ In that year,

1. *Dominion Bureau of Statistics, 1966 Corporation Financial Statistics, Queen's Printer, Ottawa, May, 1969.*

using data compiled by D.B.S., it is calculated that the Canadian rubber industry realized a return of 7.3 percent on invested capital, while companies engaged in the production of industrial chemicals recorded an average return of 6.5 percent: as noted earlier *Polymer's* 1966 return was 8.6 percent.

No conclusions can be reached on the basis of the Canadian and American industrial data referred to above since insufficient samples are available. And, in fact, it would be unjustifiable to use industry-wide statistics as anything more than a broad indication of *Polymer's* performance since its operations as a synthetic rubber producer would make it relatively unique in either industry.

A more relevant standard against which to judge *Polymer's* performance - since the government is the only shareholder - is the cost of Federal Government borrowings. And, in this respect, as is shown in Table 8 below, *Polymer* has generally done very well.

TABLE 8 - POLYMER CORPORATION - COMPARISON OF RETURN ON INVESTMENT WITH AVERAGE LONG-TERM FEDERAL GOVERNMENT BOND YIELDS, 1959-68 INCLUSIVE

YEAR	(1) POLYMER RETURN ON INVESTMENT %	(2) AVERAGE FEDERAL GOVERNMENT BOND YIELD 10 YEARS AND OVER %	DIFFERENCE (1) - (2) %
1968	4.5	6.73	-2.23
1967	3.8	5.94	-2.14
1966	8.6	5.44	3.16
1965	8.5	5.22	3.28
1964	8.1	5.18	2.92
1963	8.8	5.08	3.72
1962	11.3	5.11	6.19
1961	13.9	5.04	8.86
1960	15.2	5.18	10.02
1959	6.4	5.07	1.33

Sources: *Polymer Corporation annual reports; Bank of Canada.*

It has only been in the past two years that *Polymer* has failed to return a higher profit than the government could have realized by transferring its investment in the company into securities, or - more logically - by reducing its own borrowing requirements by an equivalent amount. Although there was little possibility of this, the *Polymer* management were no less concerned about the 1967 results - which carried over, to some extent, into 1968 - than would private sector entrepreneurs have been in similar circumstances. A decline in the company's profits had not been entirely unexpected, but a drop of almost 50 percent from the 1966 level was admittedly disappointing. *Polymer's* 1967 annual report attributed the setback to a "slackening in the demand for rubber in many parts of the world", accompanied by a "further decline in the prices received for many of the company's products."¹

A partial recovery was registered in 1968 as sales rose by 12.0 percent, up by almost \$15 million over 1967, to a record high for the corporation. More significant, however, was the action taken by *Polymer* to improve the company's profitability.

The 1968 annual report, referring only briefly to efforts made to counter the profit decline experienced the previous year, noted:

1. *Polymer Corporation, 1967 Annual Report, P. 4.*

Significant cost reductions and operating improvements enabled us to increase profits despite continuing inflationary trends in costs and further decreases in the prices received for our products.¹

A little more detail, both on *Polymer's* approach to the problem and the results obtained, later appeared in the *Financial Post*, which reported:

A good part of the current sharp improvement has come from wide-ranging efficiency and cost-cutting programs put into effect over the past two years.

In the sweeping new program, management has been upgraded in certain areas, lines of responsibility widened and overall employment pared down. An 8% increase in rubber and resin production to a record 685 million pounds was realized with 7% fewer employees.²

The recovery, apparently, is continuing. In January 1969, the company announced planned capital expenditure for the current year totalling \$15.6 million, which provides for investment in "new products and activities, particularly on the Canadian scene...."³

Notwithstanding the unhappy results of 1967 and 1968, it would appear that *Polymer* will continue its recovery and again show an exemplary return on invested capital, comparable to that found among the most successful companies in the private sector. Its record to date clearly demonstrates that it has been an outstanding example of entrepreneurial success on the part of

1. *Polymer Corporation, 1968 Annual Report, P. 2.*

2. *Polymer Looking For New Products, Financial Post, May 10, 1969.*

3. *Press release, Polymer Corporation, Sarnia, January 17, 1969.*

the Canadian government and establishes it as a model against which other proprietary crown corporations might wish to measure their performance.

Compensatory Corporations
Not Comparable to the Private Sector

CANADA DEPOSIT INSURANCE CORPORATION

Created by Act of Parliament in April 1967, the *Canada Deposit Insurance Corporation* is intended to be self-sufficient while providing protection to depositors having funds in the care of the chartered banks, trust companies and similar instrumentalities. The corporation's initial capital of \$10 million was subscribed by the Federal Government; additional funds may be advanced - out of unappropriated monies in the Consolidated Revenue Fund - up to a maximum of \$500 million.

In addition to fulfilling its rôle of insurer for deposits, the corporation is expected to act as lender of last resort to insured institutions, providing liquidity in times of financial crises. Coverage is mandatory for chartered banks and federally-chartered companies which fall under the provisions of the Trust Companies Act or the Loan Companies Act and accept deposits from the general public.

Premiums charged are the greater of \$500 or 1/3 of 1% of insured deposits.¹ Annual surpluses are to be used, initially, to build up a reserve fund. A dividend "may" be declared but the size of the payment is limited to an amount equivalent to the interest expense which would have been incurred if the paid-up share capital had been, instead, a loan of \$10 million.² Normally premiums and invested capital are held in Government of Canada bonds.

Unlike other proprietary crown corporations, the *Canada Deposit Insurance Corporation* has been exempted by the Governor-in-Council, under Section 22 of the Financial Administration Act, from income tax liability.

The first annual report of the corporation, covering the nine month period from April 1, 1967 to December 31, 1967, indicated that net income of \$371,500 had been earned, representing an annual rate of return of 4.95% on invested capital.

In this particular case, management of the corporation has no scope for entrepreneurial action, being required to invest its funds in government securities which automatically impose a ceiling on potential earnings. The corporation is also one of the smallest owned by the Canadian Government, with a full-time staff of three persons at present.³

1. *The National Finances 1968-69* - Canadian Tax Foundation, Toronto, 1968, P. 192.
2. *Canada Deposit Insurance Corporation Act*, Section 33.
3. Interview, Mr. T.J. Davis, Secretary, Canada Deposit Insurance Corporation, August 26, 1969.

CANADIAN OVERSEAS TELECOMMUNICATIONS CORPORATION

The *Canadian Overseas Telecommunications Corporation* might be described as one of the "forgotten" crown corporations. Virtually ignored by the Glassco Royal Commission on Government Organization and all but overlooked in the literature of Canadian public administration, the company is neither so profitable as to be cited as an outstanding example of government enterprise nor so newsworthy as to attract the attention of the public. Only one question has been specifically directed at the corporation in the House of Commons in the past five years, indicative, to some extent, of the interest of parliamentarians in its operations.

Yet, the company fills a vital role in maintaining Canada's international communications links, particularly in respect to telegraph, telex, telephone and, more recently, satellite transmission. In this role the corporation has consistently realized profits, since its creation in 1949, and has - in the past ten years - shown steady growth in net investment and, with one exception, in net earnings. A Summary of the financial performance of the company is presented in Table 9, which follows:

TABLE 9 - CANADIAN OVERSEAS TELECOMMUNICATIONS CORPORATION,
FINANCIAL PERFORMANCE 1959-68 INCLUSIVE

YEAR	TOTAL CAPITAL INVESTMENT*	INTEREST EXPENSE	NET INCOME AFTER TAXES	RETURN ON INVESTMENT
	\$(000)	\$(000)	\$(000)	%
1968	75,648	2,433	3,991	8.5
1967	69,020	2,279	3,550	8.6
1966	67,622	2,524	2,560	7.5
1965	67,593	2,604	2,221	7.1
1964	65,779	1,687	2,385	6.2
1963	56,946	1,339	2,008	5.9
1962	43,536	921	1,665	5.9
1961	35,639	517	1,364	5.3
1960	25,179	372	948	5.2
1959	14,639	446	626	7.3

* Includes shareholder's and equity (Gov't of Canada) and long term government loans.

Source: Canadian Overseas Telecommunications Corporation Annual Reports 1958-69.

Inasmuch as Canadian Overseas Telecommunications Corporation is in a monopoly position in Canada for the great majority of its services, it is impossible to measure its performance against equivalent private sector operations.* However, comparisons can be derived with the yield on long term Federal Government bonds which is a relevant measure of the company's performance insofar as the government is the sole shareholder. On this basis, as can be noted in Table 10 (page 67), Canadian Overseas Telecommunications Corporation has performed creditably.

* Two other companies, Anglo-American Telegraph (a subsidiary of Western Union) and the Commercial Cable Company (an ITT World Communications Affiliate) compete in minor respects with COTC but financial data for Canadian operations are not available from the U.S. parent companies.

TABLE 10 - CANADIAN OVERSEAS TELECOMMUNICATIONS CORPORATION -
COMPARISON OF RETURN ON INVESTMENT WITH AVERAGE
LONG-TERM FEDERAL GOVERNMENT BOND YIELDS, 1959-68
INCLUSIVE

YEAR	(1) C.O.T.C. RETURN ON INVESTMENT %	(2) AVERAGE FEDERAL GOVERNMENT BOND YIELD 10 YEARS AND OVER %	DIFFERENCE (1) - (2) %
1968	8.5	6.73	1.77
1967	8.6	5.94	2.66
1966	7.5	5.44	2.06
1965	7.1	5.22	1.88
1964	6.2	5.18	1.02
1963	5.9	5.08	.82
1962	5.9	5.11	.79
1961	5.3	5.04	.26
1960	5.2	5.18	.02
1959	7.3	5.07	2.23

Sources: Canadian Overseas Telecommunications Corporation annual reports; Bank of Canada.

In each of the past ten years, the company has earned a return on the government capital invested which exceeded the average yield on Federal Government long term bonds. This is a satisfactory result and is indicative of responsible pricing policies - which obviously stop short of maximizing profits, despite the almost total monopoly that the company enjoys. While, in this respect the profits cannot be regarded as particularly entrepreneurial, they are perhaps exemplary for a government company in a monopoly rôle and compare favourably - in percentage terms - with those of Bell Canada¹ which enjoys a

1. *Bell Canada 1968 Annual Report, P. 16 (Return on investment 6.9 (1968); 6.8 (1967); 6.5 (1966); 6.6 (1965)).*

similar market position in another segment of the communications field.

CENTRAL MORTGAGE & HOUSING CORPORATION

Central Mortgage & Housing Corporation was established in 1945, with capital of \$25 million, to administer the National Housing Act.

The corporation is required to underwrite, as an insurer, all loans issued by participating lenders under the NHA and, without providing competition with approved lenders, to act as a residual source of funds for persons unable to obtain NHA mortgages through normal sources. *CMHC* also has responsibilities in respect to public and student housing, urban renewal, land assembly, sewage treatment projects, housing research and community planning. In addition, the corporation is empowered to act jointly with provincial agencies in the design, planning and construction of specialized housing.

Until June 27, 1969, when the Act was amended to provide for a "free floating" mortgage rate governed solely by money market conditions, loans under the NHA were made at a ceiling of $2\frac{1}{4}$ percent above the yield on long term Federal Government bonds, adjusted every three months. The corporation plans for profits on its direct loans which amounts to the difference between the rate at which it borrows its investable funds from the Federal Government - approximately $1/8$ of one percent above the current long term bond yield rate - or

roughly two percent on all mortgages. All profits so realized are credited to the Receiver General.

However, the government in turn reimburses CMHC for the cost of its non-compensatory functions arising out of its participation in public housing, urban renewal, sewage treatment financing, etc. Such payments generally exceed the level of the corporation's profits plus income taxes but it would appear that the marketing of insured mortgages and CMHC's own lending activities raise funds which, to a considerable degree, support the financing of works carried out under the requirements of public policy.

The corporation has never failed to realize an operating profit on NHA housing loans. As illustrated in Table 11 below, CMHC's earnings are relatively stable; however, these fall considerably below the yield on long-term government bonds.

TABLE 11 - CENTRAL MORTGAGE & HOUSING CORPORATION - RETURNS ON INVESTMENT 1959-68 INCLUSIVE

YEAR	TOTAL INVESTMENT \$(ooo)	INTEREST PAID ON BORROWINGS \$(ooo)	PROFIT \$(ooo)	TOTAL RETURN TO RECEIVER GENERAL \$(ooo)	RETURN %
1968	3,876,319	187,594	11,659	199,254	5.1
1967	3,484,353	152,678	10,081	162,758	4.7
1966	2,800,785	121,359	9,335	130,694	4.7
1965	2,341,646	100,382	10,038	110,420	4.7
1964	2,069,564	87,956	8,645	96,601	4.7
1963	1,867,519	79,280	10,115	89,395	4.8
1962	1,806,421	73,375	10,452	83,827	4.6
1961	1,667,085	64,572	10,531	75,103	4.5
1960	1,471,888	52,660	10,103	62,673	4.3
1959	1,222,526	37,823	9,554	47,376	3.9

Source: Central Mortgage & Housing Corporation

There is little likelihood that *CMHC* would ever bring its profits up to a level comparable to the yield on long term Federal Government bonds without adversely affecting the supply of housing for middle and lower income groups in Canada. To do so, in fact, would defeat the purpose of the National Housing Act which, as noted earlier, provides the *raison d'etre* for *CMHC*'s existence. Recognizing this, the corporation's objectives are stated to be "To operate at minimum expense and not in an uneconomic range."¹

Given the limitations implied by the National Housing Act it is clear that *CMHC* cannot be regarded as an entrepreneurial undertaking but is, in essence, an effective instrument, organized along corporate lines, for carrying out government housing policy. As such, it cannot be compared either to its sister crown corporations such as *Polymer*, *Eldorado* and *Canadian Overseas Telecommunications Corporation* or to private sector mortgage agencies.

EXPORT CREDITS INSURANCE CORPORATION

Export Credits Insurance Corporation, which is now in the process of being replaced by *Export Development Corporation** provides an essential service to Canadian exporters without cost

1. Interview, Messrs. H.C. Linkletter, Vice-President and R.W. Desbarats, Comptroller, *CMHC*, March 10, 1969.

* First Reading, March 21, 1969, Second Reading, April 14, 1969.

to the public purse. The corporation has two rôles: insuring of Canadian goods exported to foreign customers, either at its own risk, or in exceptional circumstances involving national interest, at the risk of the government, and the extension of credit to foreign buyers of Canadian exports. It has no competition in Canada in respect to its insurance operations nor in the field of export financing - for periods in excess of five years - where it is the only Canadian source.

Export Credits Insurance Corporation is not profit-oriented. The corporation's earnings objectives have been explained in a recent speech by its president, Mr. H. T. Aitken:

....ECIC is required to operate without expense to the Canadian taxpayer. It does not subsidize the exporter, but provides a service at a very low premium. It is a self-supporting, non-profit organization. It is not in competition with any Canadian commercial enterprise....We try to operate so as just to break even, with a sufficient reserve to meet possible claims for future losses.¹

The corporation's success in providing low-cost insurance is indicated by the fact that current premium rates - which are kept confidential for diplomatic reasons - are less than half the level charged when *ECIC* first began operations in 1944.² In part, this accomplishment can be attributed to

1. Aitken, H.T., *Speech to Air Industries Association of Canada Annual Meeting, October 10, 1968, Seignory Club, Montebello, Quebec.*
2. *ibid.*

the favourable claims experience achieved by the corporation. *ECIC* has paid out only \$14.9 million in claims since its inception and has recovered \$11.5 million of this amount. Of the remaining \$3.4 million only \$887,000 has actually had to be written off; the corporation expects to eventually recover \$2.5 million from its current outstanding claims.¹

ECIC's ability to maintain a low profit margin, while avoiding significant operating losses on its insurance accounts, has also been an important factor in achieving its current low rate structure. The corporation has kept its earnings levels to a minimum, with the result that its earned surplus, accumulated over 24 years of operation, totalled only \$4.3 million at the end of 1968; a further \$6.0 million has been transferred to an underwriting reserve. *ECIC*'s performance over the past six years illustrates the success of its management in charting a course between narrow profit and loss parameters.

TABLE 12 - EXPORT CREDITS INSURANCE CORPORATION - FINANCIAL RESULTS, 1962-68 INCLUSIVE

<u>YEAR</u>	<u>NET INCOME</u> \$(ooo)	<u>LONG TERM DEBT</u> \$(ooo)	<u>CAPITAL & RESERVE</u> \$(ooo)	<u>RETURN ON TOTAL INVESTMENT</u> %
1968	427	221,179	20,271	0.2
1967	(-867)	179,576	19,843	(-0.4)
1966	314	151,180	20,710	0.2
1965	1,338	113,646	20,397	1.0
1964	1,465	72,878	19,719	1.6
1963	865	39,037	18,254	1.5
1962	896	23,130	17,390	2.2

Source: *ECIC* annual reports 1963-68

1. *Export Credits Insurance Corporation, 1968 Annual Report, P. 7.*

While the corporation has succeeded in breaking even on its insurance accounts, its financing activities are, to some extent, currently subsidized by the public purse. ECIC has charged interest at six percent on loans of five to 20 years duration at least up until the end of 1968 despite the fact that the corporation, in its descriptive literature, states: "The rate of interest is based on the cost of borrowing money to the Canadian Government."¹ In 1968 the average Federal Government long-term bond yield averaged 6.73 percent.² The explanation for ECIC's failure to increase its interest rates to reflect economic conditions in Canada may be in the competition prevalent among exporting countries in respect to credit terms that each is prepared to offer foreign buyers. The corporation and similar companies from nineteen other countries are members of the *Union d'Assureurs des Crédits Internationaux (Berne Union)* - an international association of export credit insurers. The union provides for the exchange, among its members, of credit terms currently being granted in international trade and the corporation has advised the author that "...ECIC, or any other member, will normally match credit terms sanctioned by another member."³ The fact that interest rates in some member countries, particularly West Germany, have

1. *Export Credits Insurance Corporation, What it is and How it Operates*, P. 20 (pamphlet).
2. *Bank of Canada*.
3. *Mr. J.A. Strang, ECIC, in letter dated March 4, 1969.*

not risen as rapidly as have those in North America during recent years probably has a suppressing effect on the level of interest that can be charged by the corporation. Until 1968 ECIC was able to maintain at least some margin of profit between the rate of interest incurred by the government and the level of its interest charges on financing accounts. However, during the corporation's past fiscal year, while the yield on long term government bonds rose to an average of 6.73 percent, ECIC increased its financing by \$31.7 million. The differential of .73 percent on this amount represents a loss on financing accounts of approximately \$230,000 for the year.

Although this amount is hardly significant in respect to the importance of Canada's export trade, perpetuation of the six percent rate will lead to even greater annual shortfalls. If such a subsidy, which is a direct benefit to foreign buyers and an indirect benefit to domestic industry engaged in that area of export trade requiring long term financing, is necessary, Parliament should be provided an opportunity to express its approval through annual votes of appropriations.

Moreover, while it is true that ECIC operates without direct cost to the taxpayer, as noted in Mr. Aitken's speech, the corporation, in returning a profit amounting to less than the potential yield on its capital, involves a substantial opportunity cost,* equivalent to the difference

* *i.e., The dollar amount that would be derived from the employment of a similar investment in the best alternative use.*

between the return which might be expected on the government's investment and that actually realized by *ECIC* in its annual operations. An estimate of the amount of the opportunity cost incurred in each of the past six years appears in Table 13 below.

TABLE 13 - ESTIMATED OPPORTUNITY COST OF *ECIC* TO GOVERNMENT OF CANADA, 1962-68 INCLUSIVE

YEAR	(1) TOTAL FEDERAL GOV'T CAPITAL INVESTMENT \$(ooo)	(2) AVERAGE YIELD ON LONG-TERM FEDERAL BONDS %	(3) THEORETICAL GOV'T EARNINGS i.e. (1)x(2) \$(ooo)	(4) ACTUAL <i>ECIC</i> EARNINGS \$(ooo)	OPPORTUNITY COST (3)-(4) \$(ooo)
1968	241,450	6.73	16,250	427	15,823
1967	199,419	5.94	11,845	(-867)	12,712
1966	171,890	5.44	9,351	314	9,037
1965	134,043	5.22	6,997	1,338	5,659
1964	92,597	5.18	4,797	1,465	3,332
1963	57,291	5.08	2,910	865	2,045
1962	40,520	5.11	2,071	896	1,175

Source: *Export Credits Insurance Corporation annual reports; Bank of Canada*

It should be noted that the estimate of opportunity costs derived in Table 13 is based on the government merely reducing its annual borrowings by the amount of its total investment in *ECIC*. As such it is to be considered conservative since the best alternative use of these funds would be in a much higher yield investment. Also, although the opportunity costs cited above may be considered to have been incurred in each of the years referred to, the sale or liquidation of *ECIC* to free the government's investment would not result in an annual saving approximately equivalent

to the values indicated: the saving would only be realized in the one year in which the action might be taken.

The importance of *ECIC* to Canadian export trade is such as to make it most unlikely that the government could, or indeed should, retreat from this field of activity. However, possibilities appear to exist for increasing the corporation's return on its investment without adversely affecting Canada's export position. Certainly the fact that *ECIC*'s current premium rates are now below the level charged in 1944 - despite the considerable inflation in other costs that has taken place over the past 25 years - implies that a rate increase could be implemented without undue hardship to exporters. And consideration might be given to selective subsidization of interest rates for export financing, granting a lower level in cases where it is necessary if a sale is to be obtained but charging a market rate on commodities where the seller enjoys a clear competitive advantage.

While it is recognized that this corporation was not established with entrepreneurial objectives in mind, the failure to assess reasonable charges against users of the service provided results in a potential misallocation of public resources. In short, employing investment capital in this area of activity when the yield falls below the cost to the government of borrowing equivalent funds, deprives taxpayers of benefits that could otherwise be enjoyed. And, in an entrepreneurial

sense, the failure to recognize the potential earnings power of *ECIC* to date constitutes an overlooked opportunity.

NORTHERN TRANSPORTATION COMPANY LTD.

Acquired by the Federal Government in the expropriation of its parent company, *Eldorado Gold Mines Ltd.* in 1944, *Northern Transportation Company Ltd.* is a subsidiary crown corporation of *Eldorado Nuclear Ltd.* Originally operated to serve *Eldorado's* Port Radium mine on Great Bear Lake, the company has grown into a major common carrier operation serving the Mackenzie River watershed and the Arctic coast. Reflecting this evolution, *Northern Transportation*, since 1965, has reported to Parliament through the Minister of Indian Affairs and Northern Development whereas *Eldorado* reports through the Minister of Energy, Mines and Resources.

Northern Transportation is a rarity in Canadian public enterprise at the federal level inasmuch as its development has included the takeover of its privately-owned competition. This is particularly ironic in that it contrasts sharply with the experience of its parent company which, as noted earlier, was forced by ministerial directive to stop pursuing its program of mineral exploration in competition with the private sector.

The company has apparently followed a policy of aggressive competition which led the Commons Special Committee

on Research to observe, in 1961, that:

.....Your committee heard representations from officers of Yellowknife Transportation Company and Arctic Shipping Company, and heard undenied allegations that Northern Transportation Limited took advantage of its status to obtain a preferred position in transportation in the Western Arctic and Mackenzie River Basin.¹

Although Arctic Shipping had made a tentative offer to buy Northern Transportation in 1960, both it and Yellowknife Transportation were acquired by NTCL in 1962.²

There is some evidence to suggest that the company enjoyed advantages not available to private sector companies, especially in respect to obtaining D.E.W. line cargo shipments. The president of Arctic Shipping expressed some bitterness in his appearance before the Special Committee on Research, complaining about favouritism shown to NTCL:

I would like to point out that the Canadian Maritime Commission will not allow registration in Canada of U.S. ships, purchased by Canadians, if such ships are over 5 years old. Ships presently in use by Northern Transportation: specifically, 3 U.S. Navy LST's and 3 U.S. Navy A.D.G. type tankers over 5 years old, were placed under Canadian registry. It is my understanding that this was accomplished through the issuance of orders-in-council. I might add, for the information of this committee, that Arctic Shipping Ltd. was emphatically refused Canadian registry when the company applied for admission into Canada of a similar type of ship.³

The statement was not refuted by officers of Northern Transportation who were present at the Committee meetings.

1. *Minutes of Proceedings, Special Committee on Research, Fourth Report, 1961, P. 1339.*
2. *ibid, P. 628.*
3. *ibid, P. 617.*

Following the acquisition of its competitors, the president of *NTCL*, in the company's 1965 annual report, drew attention to freight rate charges in the area served by *Northern Transportation*, and noted:

*It is significant that freight rates within the Mackenzie Basin are now 40 percent below the maximum permissive levels established by the Board of Transport Commissioners between 1948 and 1951, and that rates for shipment to points along the Arctic coast and within the Arctic islands have dropped by 25 percent since 1958.*¹

The elimination of competition to *NTCL* has made it impossible to compare the company's profit performance with private sector companies engaged in the same field. The short season on the Mackenzie and in the Western Arctic make the company's operations virtually unique, rendering irrelevant any comparison of *NTCL*'s financial results with other, more southerly-based, Canadian shipping companies.

Northern Transportation's earnings performance over the past 10 years, however, is not impressive by any criterion, as illustrated in Table 14 (page 80). Yet there are indications that the company is on the threshold of a substantial improvement in its earnings. The *NTCL* 1968 annual report, citing the surge in activity in the north, particularly at Prudhoe Bay and the North Slope in Alaska, the lower Mackenzie and the Arctic islands in Canada, noted that total revenues for the year had risen by 34 percent while tonnage rose 24.5 percent and ton-mile utilization was up by 93 percent. In

1. *Northern Transportation Company Ltd., 1965 Annual Report, P. 1.*

anticipation of further substantial growth the company is adding three new tugs and 24 sea-going barges of 1000 tons capacity to its fleet, at a cost of approximately \$11.5 million - more than doubling *NTCL*'s current total investment.

TABLE 14 - NORTHERN TRANSPORTATION COMPANY LTD. - FINANCIAL PERFORMANCE, 1959-68 INCLUSIVE

<u>YEAR</u>	<u>TOTAL INVESTMENT</u>	<u>NET INCOME</u>	<u>RETURN ON INVESTMENT</u>
	\$ (ooo)	\$ (ooo)	%
1968	7,757	194	2.5
1967	7,562	59	0.8
1966	7,503	106	1.4
1965	7,397	449	6.1
1964	6,949	518	7.5
1963	6,431	271	4.2
1962	6,159	132	2.1
1961	6,027	253	4.2
1960	5,723	60	1.0
1959	5,713	84	1.5

Source: *Northern Transportation Company Ltd.*, annual reports, 1959-68.

The service role filled by *NTCL*, in providing common carrier water transport, has become even more vital since it assumed a virtual monopoly position in the Mackenzie River and Western Arctic. There are indications that the company has - perhaps in recognition of its importance to the economic development of the region - held its rates below permissible levels which would have allowed a greater return on the capital invested. Mention was made of the company's hopes of holding the line on rates in both the 1966 and 1967 annual

reports when the company's profits represented returns of 1.4 and 0.8 percent respectively. While there is no reference to any government directive in this respect, it is rather surprising that *NTCL* would not have taken action to increase its revenues in 1966, when its profits were down sharply from the previous year, or in 1967 when it narrowly avoided a net loss on its year's operations.

If the optimism demonstrated by the company's management is borne out by experience, *Northern Transportation* may prove to be a particularly attractive investment for the government. If not, the company's operations must be regarded as indirectly subsidized insofar as it will not likely - without substantial rate increases - be able to return sufficient earnings to even match the yield expected from an equivalent investment in government bonds.

ANALYSIS OF GROUP II PROPRIETARY CROWN CORPORATIONS

Non-Compensatory Corporations Comparable to the Private Sector

CANADIAN NATIONAL RAILWAYS

As noted earlier, *Canadian National Railways* was the first major crown corporation to be established by the Federal Government. Employing more people than any other crown

company - approximately 85,240¹ - it represents the largest individual corporate investment commitment of the Canadian Government.

Much more than just a railway, *CN* is really a comprehensive transportation system, encompassing 32 incorporated companies,² excluding its aviation subsidiary, *Air Canada*. Its rail lines cover Canada and extend into several American states, either directly or over trackage owned by United States subsidiaries of *CN*. The company operates eleven road transport companies, two telegraph companies, a steamship and a ferry company as well as holding companies, bridge and tunnel investments and shares, with *Canadian Pacific Railway*, in the ownership of *CN-CP Telecommunications*. The corporation also provides transportation consulting services to foreign governments, under its *International Consulting Division*.³

Yet, with its current financial structure *CN* constitutes one of the most demanding burdens on the Federal Treasury, requiring substantial annual appropriations to meet its debt service obligations. Since 1958, *CN* has been voted more than \$432 million in payments to cover its annual deficits.⁴ During this period, the company has incurred a total interest

1. *Canadian National Railways, 1968 Annual Report, P. 46*
2. *ibid, P. 32.*
3. *ibid, P. 22.*
4. *ibid, P. 46.*

expense of almost \$624 million. Return on investment calculations, expressing net income before interest expense as a percentage of equity and long-term debt, illustrate that the company's plight is, at best, unenviable.

TABLE 15 - CANADIAN NATIONAL RAILWAYS - RETURN ON INVESTMENT
1959-68 INCLUSIVE

<u>YEAR</u>	<u>EQUITY</u>	<u>LONG-TERM DEBT</u>	<u>NET INCOME BEFORE INTEREST</u>	<u>RETURN ON INVESTMENT BEFORE INTEREST</u>	<u>INTEREST EXPENSE</u>
	\$ (ooo)	\$ (ooo)	\$ (ooo)	%	\$ (ooo)
1968	1,923,444	1,919,561	41,274	1.08	70,451
1967	1,893,072	1,884,712	29,183	.77	65,052
1966	1,875,772	1,772,840	40,109	1.09	64,702
1965	1,847,554	1,778,440	28,545	.78	61,960
1964	1,821,589	1,780,190	23,934	.66	62,660
1963	1,796,866	1,791,253	21,190	.59	64,204
1962	1,772,476	1,842,345	13,579	.37	62,498
1961	1,749,173	1,837,670	(4,832)	(-.13)	62,476
1960	1,725,642	1,828,330	(6,474)	(-.18)	61,023
1959	1,728,413	1,686,743	5,210	.15	48,798

Source: Canadian National Railways, annual reports 1959-68.

The present CN difficulties may be traced back to the origins of the crown corporation. The product of an amalgamation of several smaller railroad companies, both government and privately owned, which were in financial difficulties, CN was required to assume the debts of its predecessors. Moreover, the servicing of the outstanding debts was made a direct charge on the revenues of the company. Under such requirements CN was unable to accumulate retained earnings to finance expansion

while, in the words of a former president of the company, "...the methods used for depreciating the assets did not provide adequate depreciation reserves."¹

As a result, the company went more and more heavily into debt, requiring partial re-financing in both 1932 and 1951. The most recent adjustment carried out by the *Canadian National Railways Capital Revision Act of 1952*, though not actually writing off any indebtedness, relieved the railway of some of its interest burden by exchanging four percent non-cumulative preferred stock for \$736.4 million in interest bearing securities. This amount represented 50 percent of the total indebtedness to the public and the federal government outstanding at the end of 1951. Since that time, however, CN's long-term debt has more than doubled.

It is interesting to note that complete elimination of the present outstanding long-term debt would result in an approximate doubling of the company's return on investment. The new level of earnings which might result would, nonetheless, still be unimpressive, based on the performances of the past ten years. Recalculation of CN's 1968 income results, which produced a yield of 1.08 percent on investment before deducting interest expense, resulted in a yield of 2.1 percent if all long-term debt was totally written off.

1. *Gordon, Donald, CN - A Business Enterprise, Speech to American Association of Railroads, October 13, 1965.*

Under the present financial structure the entire amount of the company's net income is applied to its debt service obligations, with the balance of its interest expense being met by appropriations. This again does not allow for the accumulation of retained earnings and, with the acquisition of new equipment, CN will continue to go further into debt.

The essential nature of *Canadian National Railways'* function in the Canadian economy requires that it continue to compete both with other railways, particularly *Canadian Pacific*, and with other modes of transportation. Forgiveness of the debt burden, while not the complete answer, would improve the company's performance to the point where additional measures, principally the elimination of uneconomic lines now maintained at considerable expense, might lead to a narrowing in the gap between CN's earnings on total equity and that of CPR - currently estimated to be approximately 3.4 percent on its railway operations.¹

While Musolf² and others³ have expressed doubts as to whether CN and CPR can be compared, the existence of a publicly-owned enterprise, operating in the same field as a thriving private company, invites contrasts even if the ingredients of each firm are essentially different. In this respect, one can understand the sentiment behind the following

1. New Rail Rationalization Formula Generous But Tough,
Financial Times, August 18, 1969.
2. Musolf, Lloyd D., Public Ownership & Accountability,
Harvard, Cambridge, 1959, P. 20
3. See also *Royal Commission on Transportation, 1951 Report,*
Pp. 193-194.

remarks made by Donald Gordon in referring to his hopes for improvement in CN's financial performance:

.... As I have already said, Canadian National's actual efficiency is not clearly reflected in its profit and loss account because of the debt burdens to which I have made reference. If and when CN's capital revision proposals are implemented, the real accomplishments of the company and its personnel should be clearly visible. One of the results will undoubtedly be higher morale among CN officers and employees who, like their counterparts in any industry, would like to have their efforts and achievements recognized.¹

However, in some areas where statistics permit comparisons, CN's performance - on its rail operations - measures up reasonably well with that of CPR, as can be noted in Table 16 below.

TABLE 16 - RAILWAY PERFORMANCE COMPARISONS, CN AND CPR, 1962-68 INCLUSIVE

YEAR	FREIGHT REVENUE TOTAL TON MILES (BILLIONS)		FREIGHT REVENUE PER TON MILE (CENTS)		REVENUE PER PASSENGER MILE (CENTS)	
	CPR	CN	CPR	CN	CPR	CN
1968	34.6	49.7	1.39	1.43	2.72	3.45
1967	35.4	48.8	1.32	1.39	2.69	3.36
1966	38.0	49.6	1.23	1.38	2.88	3.38
1965	33.8	46.1	1.37	1.39	2.73	3.27
1964	33.9	44.5	1.32	1.36	2.44	3.21
1963	29.1	40.2	1.44	1.38	2.97	3.73
1962	26.1	35.6	1.51	1.49	3.09	4.21

Source: CN and CPR annual reports, 1963-68.

1. Gordon, Donald - CN - A Business Enterprise, Speech to American Association of Railroads, October 13, 1965.

CN appears to have enlarged its share of freight revenue ton mileage, possibly at the expense of *CPR*, registering a 40 percent improvement over the period 1962-68 while *CPR*'s tonnage increased by 32.5 percent. *CN*'s freight revenues, on a ton-mile basis, exceeded those of *CPR* in all but two years. Revenues per passenger mile were substantially higher for *CN* than for its major competitor.

On the other hand, as illustrated in Table 17, *Canadian National Railways*' financial results have not approached those of *Canadian Pacific*, at least during the past 10 years.

TABLE 17 - COMPARISONS OF FINANCIAL RESULTS, RAILWAY OPERATIONS
CN AND CPR, 1959-68 INCLUSIVE

YEAR	NET RAILWAY EARNINGS (IN MILLIONS \$)		CPR - RETURN ON INVESTMENT ON RAILWAY PROPERTY	CN - RETURN ON ALL INVESTMENT BEFORE INTEREST*
	CPR	CN	%	%
1968	41,260	18,729	3.2	1.1
1967	39,636	2,769	3.1	0.8
1966	50,220	24,268	3.9	1.1
1965	40,240	9,910	3.2	0.8
1964	43,465	7,457	3.5	0.7
1963	35,262	5,011	2.8	0.6
1962	28,978	(-5,819)	2.3	0.4
1961	37,651	(-16,225)	2.9	(-0.1)
1960	33,675	(-18,478)	2.5	(-0.2)
1959	36,046	(-6,024)	2.7	0.2

* Return on investment for *CN* is based on total *CN* results and total investment; return on investment data for *CPR* is based on railway earnings and railway investment only.

Sources: Net earnings data obtained from *CN* and *CPR* annual reports; *CPR* return on investment data supplied by Mr. P.E. Carriere, Ass't to Chairman *CPR* in letter dated March 17, 1969; *CN* return on investment data calculated from *CN* annual reports, 1959-68 inclusive.

While it is clear that comparisons between *CN* and *CPR* are at best imprecise and somewhat distorted, improvement in the financial structure of the *Canadian National Railway System* would eliminate many of the dissimilarities and facilitate a better evaluation of the relative efficiency of *CN's* rail operations. As mentioned above, elimination of the debt would be but one step in the direction of putting the railway on a sounder financial basis. However, *CN's* long term debt totalled almost \$2.0 billion at the end of 1968, of which more than \$1.1 billion is accounted for by bonds held by private individuals; the balance is made up of Government of Canada bonds and debentures.

Inasmuch as it is most unlikely that any Federal Cabinet will take action to write off *CN's* debt as long as the demands on government resources remain at the present level, realistic annual comparisons between the performances of the two railroads must be regarded as remote.

Non-Compensatory Corporations
Not Comparable to the Private Sector

CANADIAN BROADCASTING CORPORATION

The Broadcasting Act, which received Royal Assent on March 7, 1968, establishes the objectives of the *Canadian Broadcasting Corporation*, as follows:

- f) *there should be provided, through a Corporation established by Parliament for that purpose, a national broadcasting service that is pre-dominantly Canadian in content and character;*
- g) *the national broadcasting service should*
 - (i) be a balanced service of information enlightenment and entertainment for people of different ages, interests and tastes covering the whole range of programming in fair proportion.*
 - (ii) be extended to all parts of Canada, as public funds become available.*
 - (iii) be in English and French, serving the special needs of geographic regions, and actively contributing to the flow and exchange of cultural and regional information and entertainment, and,*
 - (iv) contribute to the development of national unity and provide for a continuing expression of Canadian identity;¹*

Clearly, with such a mandate, the CBC cannot be regarded as a commercial venture. Yet the corporation does exhibit some of the characteristics of private broadcasting companies. It has, for example, purchased a one-eighth interest in a film company which produces news documentaries - *Visnews Ltd. of London, England* - presumably to minimize its costs in obtaining necessary news film footage. And, more significantly, it depends on revenues from the sale of both radio and television advertising for a substantial portion of its income. Hence, it competes with private broadcasting interests for a share of the total advertising expenditure allocated to its media.

1. The Broadcasting Act, S.C. 1968, C. 25, Part I(2).

The corporation's competitive efforts in this field may be modified by the fact that expenses it incurs in fulfilling its responsibilities under the Broadcasting Act, which cannot be financed by advertising, are recoverable through parliamentary appropriations. And, indeed, it might be argued that the CBC cannot comply with its obligations to "...provide a balanced service of information, enlightenment and entertainment" and "contribute to national unity" while providing for a continuing "expression of Canadian identity" if it is also expected to maximize its advertising revenues. The Broadcasting Act itself, in fact, makes no reference to advertising and may, as a result, have introduced the possibility of eventual elimination of commercial announcements or program sponsorship.

In lieu of a clear policy statement to this effect, however, it must be assumed that the corporation is expected to raise whatever income it can through the sale of advertising time on both its radio and television stations. This assumption was certainly made by the Royal Commission on Government Organization - the Glassco Commission - which criticized the CBC's efforts in marketing its advertising and noted:

The sales force of the corporation is relatively small in comparison with its competitors. For example, a private station in Hamilton has a

*larger sales staff in Toronto than the Corporation has for national and local sales in the whole of the Toronto area.*¹

The Glassco Commission recommended that a general sales manager position be created, with responsibility for coordinating national and regional advertising sales. Although the recommendation was submitted in 1963, a review of subsequent *CBC* annual reports failed to reveal any reference to such a position though other major executives, including at least three general managers in other areas of responsibility are identified. The *CBC*, therefore, apparently has not agreed with the Royal Commission's assessment.

It is interesting to note, however, that the corporation's sales performance has not improved since the Glassco recommendation was submitted. An analysis of statistics on advertising presented in the *CBC* annual report for 1968-69 indicates that, while the corporation's volume of advertising has increased, its growth rate is much less than that achieved by private broadcasting interests. Between 1963 and 1968 inclusive, *CBC* net advertising revenues increased by 30.4 percent, from \$23 million to \$30 million. By contrast, competing private radio and television broadcasting advertising rose from \$93 million to \$180 million in the same period, up 94 percent.²

1. Report on the Royal Commission on Government Organization, Queen's Printer, Ottawa, 1963, Vol. IV, P. 46.
2. Canadian Broadcasting Corporation, 1968-69 Annual Report, Table 20, P. 72.

In part, the CBC's advertising deficiencies may result from the fact that a large percentage of all of its television programming is considered as either unsaleable or not available for sale.* But, to some extent the corporation's failings in this respect appear to reflect lack of sufficient audience appeal.

Radio and television announcement or program sponsorship rates are based on advertising demand which, in turn, varies with the number of listeners or viewers that individual stations can attract. Advertising agencies base their decision on *Bureau of Broadcast Measurement* statistics which, using sampling techniques, estimate the sizes of audiences tuned to individual stations. In Canada's two major metropolitan areas - Montreal and Toronto - CBC radio and television time rates are lower than those of their leading private station competitors, as illustrated in Table 18.

TABLE 18 - COMPARISON OF RADIO AND TELEVISION TIME CHARGES FOR 60 SECOND CLASS AA ANNOUNCEMENTS, CBC AND LEADING PRIVATE STATIONS, MONTREAL AND TORONTO, AUGUST 1969

	<u>MEDIUM</u>	<u>CITY</u>	<u>STATION</u>	<u>RATE PER 60 SECONDS</u>
<u>English Language</u>	Radio	Montreal	CBM (CBC)	\$ 26.00*
			CFCF	40.00
			CJAD	85.00
	Radio	Toronto	CBL (CBC)	45.00*
			CHUM	80.00
			CFRB	140.00
	Television	Montreal	CBMT (CBC)	275.00*
			CFCF-TV	475.00
	Television	Toronto	CBLT (CBC)	450.00*
<u>French Language</u>	Radio	Montreal	CFTO-TV	500.00
			CBF (CBC)	40.00*
			CKAC	50.00
	Television	Montreal	CJMS	95.00
			CBFT (CBC)	375.00*
			CFTM-TV	700.00

*Denotes lowest in group

Source: Canadian Advertising Rates & Data, Volume 42,
No. 8, August 1969.

* See for example, Table 18, P. 70 - 1968-69 CBC Annual Report
and Table 22, P. 40, 1966-67 CBC Annual Report

If, in fact, the *CBC* is failing to attract audiences, the problem is not one of capitalizing on opportunities for advertising sales but of programming and, possibly, of the corporation's basic objectives. *CBC* producers may be out of touch with the public, or it may be impossible to adhere to the philosophy expressed in the Broadcasting Act and still attract the largest possible audiences. In the latter case it might be more desirable to operate the *CBC* without advertising.

On the other hand, if advertising rates are not valid indicators of the popularity of radio and television stations, and the *CBC* is able to appeal to large audiences, the failure of the corporation to develop the full potential of its advertising revenues results in an unnecessary burden on the public purse.

FARM CREDIT CORPORATION

The *Farm Credit Corporation* was established as a proprietary crown corporation in 1959, replacing the *Canadian Farm Loan Board*. The corporation offers long-term mortgage loans to farmers and, under the terms of the *Farm Machinery Syndicates Act* (1964) which it administers, makes loans to groups of three or more farmers for the purchase of farm machinery for their cooperative use.

The FCC considers that its primary objective is:

To facilitate the organization of Canadian agriculture into viable farm units, in the hands of competent farmers, so that agriculture may make the greatest possible contribution to the Canadian economy, and provide farmers with equitable returns for their investment of capital, work and skills.¹

When originally established it was intended that the corporation should break even on its operations which, at that time, consisted primarily of making low-cost mortgages available to farmers.² However,, since the Act restricted interest charges on the first \$25,000 to five percent while the corporation, in its first year of operation, found it necessary to borrow at 5.13 percent there was, from the outset, very little hope that the corporation would be able to function without appropriations.

At the end of its first year, having employed government loans totalling \$110.7 million, at an average interest rate of 4.215 percent, the FCC recorded a profit of \$240,000.³ In subsequent years, however, with increased borrowings at higher rates, the average interest level rose steadily, reaching 6.41 percent by 1968, and the corporation recorded loss after loss. In 1963-64 the corporation began to obtain appropriations to cover its deficits, having seriously depleted its reserve for losses in the first four years of its operation. The results of the FCC's lending activities since its creation are presented in Table 19, which follows:

1. *Fact Sheet, Farm Credit Corporation.*
2. *Interview, Mr. S.O. Robinson, Farm Credit Corporation, March 20, 1969.*
3. *Farm Credit Corporation, 1959-60 Annual Report.*

TABLE 19 - FINANCIAL PERFORMANCE OF FARM CREDIT CORPORATION,
FISCAL YEARS 1959-60 TO 1968-69 INCLUSIVE

YEAR	(1) NET FEDERAL GOVERNMENT INVESTMENT \$(000)	(2) PROFIT OR (LOSS) \$(000)	(2)/(1)=(3) RETURN ON INVESTMENT %	(4) AVERAGE YIELD ON LONG TERM BONDS %	TOTAL LOSS ON INVESTMENT %
1968-69	41,526	(6,266)	-15.08	6.73	-21.81
1967-68	39,336	(3,809)	-9.68	5.94	-15.62
1966-67	32,086	(2,579)	-8.03	5.44	-13.47
1965-66	25,325	(1,030)	-4.06	5.22	-9.28
1964-65	18,750	(530)	-2.82	5.18	-8.00
1963-64	15,015	(1,119)	-7.45	5.08	-12.53
1962-63	12,021	(1,081)	-9.00	5.11	-14.11
1961-62	10,858	(776)	-7.14	5.04	-12.18
1960-61	9,936	(203)	-2.04	5.18	-7.22
1959-60	8,749	240	2.74	5.07	-2.33

* Total loss on investment represents the difference between the return on investment achieved and the yield paid by the gov't in borrowing an amount of capital equivalent to its net investment in the FCC.

Source: Farm Credit Corporation annual reports,
1959-60 to 1968-69

Unlike many corporations which identify interest costs as an expense on the income and expense statement, the *Farm Credit Corporation* deducts its interest obligations on government borrowings directly from its interest income. Hence it was not feasible to calculate a value for return on investment, reflecting total income (earnings plus interest) as a percentage of equity and long term debt as used elsewhere in this study. However, inasmuch as the corporation has paid the full amount

of interest assessed on each series of its loans from the government, its net income or loss results are more appropriately measured against the net government investment.

The serious deficits of the first ten years of the *Farm Credit Corporation's* existence cannot be attributed to mismanagement within the corporation but must be ascribed to the government's failure to amend the Act in recognition of the increased costs of its own borrowings. The inaction resulted in the evolution of a substantial subsidy where Parliament had intended none to exist. In 1968, for example, the total loss on the net government investment of 21.8 percent (see Table 19) amounted to \$8.8 million.

The corporation was established to offer low-cost loans and operate without appropriations. Yet, for nine of its first ten years it provided loans at less than cost and required appropriations in six successive years. Even at an early stage of its development it was recognized that the corporation was not meeting its intended obligations. Ashley and Smails, as early as 1965, noted:

*The reports of the Corporation for 1959-60 and 1960-61 drew attention to the fact that the act fixed the interest rates for corporation loans, and that it was lower than the rate the corporation was paying for government advances. The results of operations depend largely on the difference between these rates. The board reported a profit in its first year and a loss in the next two years. If the rates fixed are to continue to result in a loss on operations, it is doubtful if the corporation should continue, in Schedule D of the Financial Administration Act, as a proprietary corporation.*¹

1. Ashley, C.A. & Smails, R.G.H., *Canadian Crown Corporations*, Macmillan, Toronto, 1965, P. 153.

However, the government has recently taken steps to bring loans under the Farm Credit Act into line with the cost of its own borrowings. An amendment to the Act, which received Royal Assent on November 14, 1968, included the following sections:

16A. *The interest payable in respect of any loan made under this Act shall be at the rate or rates prescribed by the Governor-in-Council pursuant to subsection (1a) of Section 19 at the time of approval of the loan.*

19(1a) *The Governor-in-Council may from time to time by regulation prescribe the rate or rates of interest to be paid in respect of any loan made under this Act.¹*

It is intended, initially, that the FCC will charge rates which will be one percent above the cost it must pay for its borrowings. The corporation estimates that it will require approximately five to six years at the new interest level before it can begin to break even.² Presumably, the higher rates will begin to reduce the corporation's dependency on appropriations within the current year.

THE ST. LAWRENCE SEAWAY AUTHORITY

Legislation establishing the *St. Lawrence Seaway Authority* to construct, maintain and operate a deep waterway between Montreal and Lake Erie was enacted by the Canadian

1. *Bill C-110 - An Act to amend the Farm Credit Act, November 14, 1968.*
2. *Interview, Mr. R. McIntosh, Farm Credit Corporation, March 20, 1969.*

Parliament late in 1951.¹ Although Canada had announced its intention to proceed with construction of locks and channels associated with the joint navigation-power project on the St. Lawrence River by itself, an understanding was reached - in 1954 - with the United States Government on a formula which would permit American participation in the waterway. The agreement entered into between the two countries called for the recovery of capital and operation and maintenance costs for navigation facilities through tolls charges on traffic using the system, a necessary condition for the U.S. government which faced strong anti-Seaway opposition from railway and American Atlantic coast ports. A United States government company, the *Saint Lawrence Seaway Development Corporation*, was established to operate and maintain the two locks on American territory in the International Section.

Tolls committees, established by the *Authority* and its American counterpart, reached agreement on an acceptable forecast of future traffic which was expected to grow at a relatively steady rate, reaching 50 million tons of cargo by the end of the Seaway's first decade. On this basis, tolls charges were developed from estimated revenue requirements sufficient to cover operation and maintenance costs, interest expense and recovery - over a 50 year period - of invested

1. *St. Lawrence Seaway Authority Act*, R.S.C. 1952, C. 242.

capital, expected to amount to \$311 million for Canada and \$131 million for the United States.¹

Hence, with the opening of the deep-draft waterway in 1959 a toll of four cents per gross registered ton was levied on all vessels using the system, while cargo tolls were introduced, amounting to 40 cents per ton on bulk cargo goods - iron ore, grain, coal, etc. - and 90 cents per ton on general cargo, mainly manufactured goods. The tolls were to be collected jointly, revenues being shared proportionally according to preliminary estimates of respective annual charges, 71 percent initially payable to the *Authority* in Canadian funds and 29 percent, in U.S. funds, to the *Development Corporation*.

The agreement referred to above applied only to the Montreal-Lake Ontario Section of the Seaway. The *Authority*, however, was also given responsibility for operating and maintaining the Welland Canal, connecting Lake Ontario and Lake Erie. The Welland had been re-built to large vessel dimensions between 1913 and 1932 but dredging was required to adapt it to Seaway draft standards. Approximately \$27 million was expended on channel improvements,² to be recovered through tolls in the same manner as in the case of the Montreal-Lake Ontario Section. The original capital cost of the Welland Canal - \$130 million - was not included in the repayment requirement,

1. *St. Lawrence Seaway Authority, Canadian Tolls Committee, Report of the Tolls Committee, June 12, 1958, P. 3.*
2. *St. Lawrence Seaway Authority, 1959 Annual Report, P. 26.*

the canal instead was "entrusted" to the *Authority*. Tolls of two cents per gross registered ton on vessels and of two cents and five cents per ton on bulk and general cargoes respectively were thus introduced on the Welland, coinciding with the opening of the 1959 season of navigation.

Although traffic increased by 75 percent on the Montreal-Lake Ontario Section and by 29 percent on the Welland in the Seaway's first year, the totals were considerably below the forecasts upon which re-payment schedules had been based. The Welland Canal, in fact, failed to produce enough income from tolls to meet operation and maintenance expenses. The Montreal-Lake Ontario Section registered a \$5.9 million net operating income and its first season, but interest expense, at \$7.4 million, resulted in a net loss of \$1.5 million. The situation did not improve significantly over the next three years; the gap between actual and forecast tonnages and revenues widened.

The original tolls agreement between the *Authority* and the *Development Corporation* provided for a review at the end of the first five years. However, in 1962, in mid-season, the Federal Government suspended the toll charges on the Welland Canal¹ without making provision for appropriations. Interest accumulation on the section's net losses produced a total deficit of \$20.8 million by the end of 1963. Traffic rose

1. *St. Lawrence Seaway Authority, Annual Report, 1962, P. 8.*

sharply on both sections in 1964, increasing by 27 percent on the Montreal-Lake Ontario Section and 25 percent on the Welland. Nonetheless, as the Authority's 1964 annual report noted:

During 1964, a further agreement was reached to extend the developmental period by two years with no change in tolls. The joint review is being continued and at the conclusion of this two year extension, as provided by the international agreement, the intent is that tolls proposals should be related as realistically as possible to the financial requirements of the two entities.¹

In the meantime, although the Welland tolls remained suspended, the government took steps to alleviate the increasing burden of interest accumulation and operating losses on this section of the system. The 1965 annual report explained:

Early in 1965 the Authority was re-imbursed for the accumulated 1959-64 deficit of the Welland Section, which amounted to \$27.1 million, by means of a Parliamentary appropriation.²

Subsequently, in 1966, the Authority submitted a report to the Federal Government in which it advised that "...agreement was reached, for the purpose of public hearings", with the U.S. Saint Lawrence Seaway Development Corporation to

raise tolls on the Montreal-Lake Ontario section of the Seaway by approximately 10% and to divide toll revenues on a 72/28 basis rather than the 71/29 basis as at present;

introduce a \$100.00 per lockage fee, phased in over five years, on the Welland with the present cargo tolls remaining in suspension.³

1. St. Lawrence Seaway Authority, Annual Report, 1964, P. 5.
2. St. Lawrence Seaway Authority, Annual Report, 1965, P. 18.
3. St. Lawrence Seaway Authority, Report as to the Sufficiency of Seaway Tolls and Proposed Changes Related to the Financial Requirements of the St. Lawrence Seaway Authority, June 30, 1966, P. 1.

The Authority went on to conclude:

That the 10 per cent increase for the St. Lawrence Section as per the schedule is related as realistically as possible to the financial requirements of the Authority and is economically justifiable.

The Agreement entered into with respect to the sharing of tolls for the Montreal-Lake Ontario Section on a 72/28 ratio is an integral part of the general increase. It already reflects substantial concessions by Canada and the Authority feels that it represents its minimum position acceptable for five years.....

That the adoption by Canada of the per lockage fee for the Welland Canal which is related to the recovery of operation and Maintenance costs is justified and not excessive. It is the view of the Authority that this is quite properly a decision for the Canadian Government.¹

Several months later, in March 1967, the then Minister of Transport, the Honourable J. W. Pickersgill rose in the House of Commons to state:

On January 9 I tabled the report on St. Lawrence Seaway tolls prepared by the St. Lawrence Seaway Authority. I had previously indicated that the proposals in that report and in the parallel report of the St. Lawrence Seaway Development Corporation of the United States would be the subject of negotiation with the United States government and that no action on seaway tolls would be taken prior to an announcement in this House.

Discussions with the United States have now taken place and I am glad to announce that agreement has been reached on the toll arrangements which will apply to the Montreal-Lake Ontario section of the Seaway for the next four navigation seasons. Both Seaway entities proposed that the level of tolls be increased by 10 per cent and that toll revenues be divided in the ratio 72 per cent for Canada and 28 per cent for the United States in place of the

1. *ibid*, Pp. 1-2 (underscoring mine)

previous 71/29 ratio. The United States government has unfortunately not been willing to accept the proposed increase in tolls at this time but, in recognition of the relatively greater operation deficiency incurred by Canada, has agreed to an improved division of tolls revenue in the ratio 73/27 in Canada's favour for the next four seasons.

In all the circumstances and in the interest of preserving the joint arrangements we have entered into with the United States for the operation of the Seaway, which are of considerable practical advantage to Canada and to all Seaway users, the Canadian government has accepted the foregoing which means that the present level of tolls on the Montreal-St. Lawrence section of the Seaway will continue to apply through 1970.¹

The minister went on to add that the government had accepted the Authority's recommendation of a lockage fee for the Welland Canal, to be implemented in increments of \$20 per lock annually, until reaching \$100 per lock in 1971.

The short-fall in the Authority's revenues in its first decade of operations can be attributed to several factors, not the least of which was the apparently overly optimistic forecast of traffic for the first half decade, the relative price inflexibility imposed by the original agreement in providing for a tolls review only after five years of operating experience and the difficulties in securing international agreement to raise tolls despite the obvious need for increased income to meet repayment schedules. Adding to these difficulties was the fact that unionized employees of the Authority, using their considerable negotiating power while demand for Seaway shipping

1. Canada, House of Commons Debates, 1967, Pp. 13875-6.
(underscoring mine)

was at a peak, in 1966, obtained a wage settlement granting increases of 30 percent in a two year agreement. Also, strikes involving lake vessels in 1967, among Seaway workers and grain handlers in 1968, and iron ore miners in 1969 have interfered with cargo movements and, possibly, with traffic growth.

As a public enterprise investment - in terms of its own profitability - the Seaway must be regarded as a qualified success. Seen in its whole, that is, as both the Montreal-Lake Ontario and Welland sections combined, it has produced a negligible return of the government capital invested in its construction and improvements, as indicated in Table 20. In its most recent season, on a total government investment of \$511.2 million it produced income, before interest expense, of only \$4.3 million: the yield on an equivalent amount of capital invested in Government of Canada bonds at current interest rates would have amounted to \$34.4 million. Hence, in the past year alone, when unduplicated traffic through the system amounted to 66.4 million tons,¹ Canadian and international shipping using the Seaway was subsidized to the extent of 45.3 cents on every ton of cargo.

1. *St. Lawrence Seaway Authority, 1968 Traffic Report, P. 5.*

TABLE 20 - RETURN ON TOTAL GOVERNMENT INVESTMENT IN BOTH MONTREAL-LAKE ONTARIO AND WELLAND SECTIONS OF THE ST. LAWRENCE SEAWAY, 1959-68 INCLUSIVE

YEAR	(1) INCOME BEFORE INTEREST EXPENSE \$(millions)	(2) TOTAL GOVERNMENT INVESTMENT \$(millions)	(3)=(1)/(2) RETURN ON INVESTMENT %	(4) YIELD ON LONG TERM GOVERNMENT BONDS %	TOTAL LOSS ON INVESTMENT (4)-(3) %
1968	4.3	511.2	0.84	6.73	5.89
1967	3.2	481.7	0.66	5.94	5.28
1966	3.0	455.4	0.65	5.44	4.79
1965	3.6	424.4	0.84	5.22	4.38
1964	4.6	406.4	1.13	5.18	4.05
1963	3.1	396.7	0.78	5.08	4.30
1962	2.4	370.1	0.64	5.11	4.47
1961	2.8	353.6	0.79	5.04	4.25
1960	2.8	330.3	0.84	5.18	4.34
1959	4.6	308.7	1.49	5.07	3.58

Sources: St. Lawrence Seaway Authority, 1968 Annual Report; Bank of Canada.

Yet, the inclusion of Welland Canal results in any assessment of the Seaway's financial performance could be disputed. Tolls on this section of the waterway were suspended by the government in July, 1962, and remained that way until the lockage fee was introduced in 1967. Even before the suspension there was evidence to suggest that the Welland toll rates were too low to meet operation and maintenance costs, much less repay capital and interest on dredging to Seaway draft. And it must be remembered that the Welland was approximately 30 years older in service and 50 years older in design than the Montreal-Lake Ontario Section. As such, it required a considerable expenditure, especially in the years following 1963, for modernization.

If Welland revenues and expenses are deleted, the return on investment performance for the Montreal-Lake Ontario Section approaches a level corresponding roughly to one-half of the yield on long term government bonds. In 1968, income before interest expense amounted to \$12.6 million on a total government investment of \$390.0 million, or 3.23 percent, as detailed in Table 21. An equivalent capital outlay on government bonds would have returned \$26.5 million. The difference, pro-rated against shipments through this section of 48.0 million tons last year, represents a subsidy of 29.0 cents per cargo ton to both Canadian and international shipping using the system.

TABLE 21 - RETURN ON CANADIAN GOVERNMENT INVESTMENT IN MONTREAL-LAKE ONTARIO SECTION OF THE SEAWAY, 1959-68 INCLUSIVE

YEAR	(1) INCOME BEFORE INTEREST EXPENSE \$(millions)	(2) TOTAL GOVERNMENT INVESTMENT \$(millions)	(3) $-(1)/(2)$ RETURN ON INVESTMENT %	(4) YIELD ON LONG TERM GOVERNMENT BONDS %	TOTAL LOSS ON INVESTMENT (4) - (3) %
1968	12.6	390.0	3.23	6.73	3.50
1967	11.4	383.6	2.97	5.94	2.97
1966	13.1	375.2	3.49	5.44	1.95
1965	11.7	370.8	3.15	5.22	2.07
1964	10.0	362.8	2.80	5.18	2.38
1963	7.2	356.7	2.01	5.08	3.07
1962	5.4	337.1	1.60	5.11	3.51
1961	5.0	321.2	1.55	5.04	3.49
1960	4.5	300.6	1.49	5.18	3.69
1959	5.3	283.4	1.87	5.07	3.20

Sources: *St. Lawrence Seaway Authority, 1968 Annual Report;*
Bank of Canada.

The Seaway, of course, has wider importance than its own profitability. Its construction made it economic to develop the large iron ore deposits of Northeastern Quebec and Labrador, which has resulted in a substantial export trade into U.S. Great Lakes ports. Also, the rate for shipping grain has been sharply reduced. In 1958, the last year of operation of the old shallow draft and under-sized St. Lawrence Canals, the rate for shipping grain from the Lakehead to Montreal amounted to \$5.33 per ton, or 16.0 cents per bushel:¹ last year the rate, which now includes all Seaway tolls, dropped as low as \$2.66 per ton - eight cents per bushel.² And it is a matter of speculation as to whether the alternate Canadian transport modes could have handled the shipment of the several million tons of grain exported to Russia, within the deadline imposed, without the Seaway.

Yet, the substantial costs involved in the construction and operation of the Seaway justify user charges, particularly since it is an international waterway and much of the traffic using the system is comprised of foreign ocean vessels. Moreover, the National Transportation Act has defined current Canadian government policy in this respect by requiring that:

...each mode of transport, so far as practicable, bears a fair proportion of the real costs of the resources, facilities and services provided that mode of transport at public expense.³

1. Dominion Bureau of Statistics, Grain Trade of Canada, 1966-67, P. 119.
2. Dominion Bureau of Statistics, Grain Trade of Canada, 1967-68, P. 109.
3. Statutes of Canada, 1966-67, C. 69, Section 1(b), P. 595.

An increase in the tariff of tolls can be proposed in 1970 for implementation in 1971. Whether such an increase, coupled with growing traffic, will enable the Authority to overtake its rising debt structure and meet its repayment target date in 2009 remains to be seen. Certainly a tolls increase of even 10 percent in 1967, as recommended by the Canadian and American operating entities, would have helped to arrest the growing interest burden on unserviced debt.

The present tariff of tolls on the Montreal-Lake Ontario Section has remained unchanged since 1959 despite substantially increased labour and materials costs over the past decade. Indeed, since the devaluation of the Canadian dollar in 1962 and the adjustment in the sharing ratio from 71 percent Canadian funds to 73 percent in 1967, the cost of using the Seaway has actually decreased for international shipping using U. S. currency.

CHAPTER IV

WEAKNESSES OF CROWN CORPORATIONS

Private corporate enterprise, with its relationship between management, board of directors and shareholders, possesses a hierarchy of responsibility and accountability for which no exact counterpart can be recognized among crown corporations. Although all but one of the public enterprise firms examined in this study have boards of directors,* the character of such boards varies considerably from corporation to corporation.

Directors of some government companies, notably the *Canada Deposit Insurance Corporation* and *Export Credits Insurance Corporation* are drawn exclusively from the ranks of senior civil servants. Other boards, including *Central Mortgage and Housing Corporation* and the *Farm Credit Corporation*,** have mixed composition, consisting of senior civil servants, professional, regional and sectoral representation. The business-oriented

* *The St. Lawrence Seaway Authority, with a full-time triumvirate comprised of the president and two members, one of whom acts as vice-president, does not have a board of directors.*

** *The Farm Credit Corporation's "Members of the Corporation", although not specifically designated as a board of directors, apparently functions as such since only the chairman and the vice-chairman act on a full time basis. The other three members consist of the Deputy Minister of Finance, the Assistant Deputy Minister, Production and Marketing, Department of Agriculture, and the Assistant Deputy Minister, Rural Development, Department of Forestry and Rural Development. The FCC has an advisory committee comprised of nine regional agricultural experts, representing eight provinces.*

crown corporations - *Air Canada*, *Canadian National Railways*, *Eldorado Nuclear*, *Northern Transportation* and *Polymer* - have directors with qualifications of expertise in private enterprise, although both *Air Canada* and *CN* appear to have regional representatives as well. Alone among all of the crown corporations, the *Canadian Broadcasting Corporation's* board of directors is comprised, aside from the president, of 14 men and women - from all provinces except New Brunswick, Newfoundland and Prince Edward Island - representing the general public.

In the private sector, in theory at least, a board of directors represents the shareholders and is accountable to them for the performance of the company. Government enterprise, however, poses difficulties in this respect, particularly in Canada where all directors of crown corporations - most for stipulated terms on a "during pleasure" basis - are appointed by the Governor-in-Council on recommendation from the cabinet. In this respect it might appear that the cabinet functions as shareholder. However, it lacks the basic qualification of ownership and only accepts dividends or provides funds on behalf of Parliament. Moreover, ministers to whom crown corporations report are responsible to parliament for the activities of these government companies. Also, some crown corporations, particularly the *CBC* and *CN*, report through the minister to Parliament, implying that the body which, in most instances, created the corporation has the rights of

shareholders, acting as a trustee for taxpayers who, willingly or otherwise, financed the enterprise.

There are, on the other hand, reasons to doubt the validity of this assumption, as Hodgetts has noted:

...corporations have shown a cavalier disregard for the shareholders in refusing, for example, to answer questions. Moreover, in most important matters, particularly financial, Parliament has shrugged off its normal responsibilities. Parliament, then, is left with the unenviable task of trying to re-introduce itself into an area from which it has agreed in the originating statute to withdraw. In these circumstances, forthright assertion of the shareholders' function is regarded as "intervention" and Parliament accordingly tends to gyrate between alternative fits of despairing passivity and bursts of energetic but uninformed criticism.¹

Indeed, Members of Parliament, particularly those in opposition, must find crown corporations a source of considerable frustration in trying to obtain information on their activities. An example of the difficulties faced by parliamentarians in this regard is illustrated by the recent experience of one opposition M.P.:

....I shall refer the House to the answer to question No. 53 which I had put on the order paper in order to learn how many senior civil servants were earning \$17,000 and more.

At Polymer Corporation ... I was given the following answer, and I quote:

"Polymer does not have any civil servants in its employ."²

1. Hodgetts, J.E. - The Control of Public Enterprise in Canada, International Political Science Association, Rome Congress, Circa 1959, P. 13
2. Canada, House of Commons Debates, December 12, 1968, P. 3878.

Later, in response to a question on bilingualism among such employees, *Polymer* replied:

*The corporation would not wish to furnish the information requested as disclosure of the number of employees earning \$17,000 and more ... (and are bilingual) ... would not be in the best interests of the company.*¹

To some extent crown corporations may be justified in refusing to provide information which could jeopardize their competitive position or which might endanger employee morale. Yet crown corporation employees are public servants, at least insofar as their companies are owned by the government, acting on behalf of the people. And not even private enterprise can afford the luxury of arrogance such as was shown by *Polymer* in replying that it had no "civil servants". The refusal to disclose information without substantial reason can hardly be endorsed, particularly when the request is made by a Member of Parliament. And while it may be true, as one leading industrialist on *Polymer's* board of directors has said:

*.....we believe - without reservation - that an important contribution to *Polymer's* success has been the freedom from what I might call "political pressure".*²

such freedom is not encouraged by an attitude of distaste towards representatives of the corporation's shareholders.

Arthur Meighen may have set the precedent for the tradition of detachment which has evolved around crown

1. *ibid*, P. 3878

2. *Standing Committee on Public Accounts, Minutes of Proceedings and Evidence No. 11, May 9, 1961, P. 327 (Mr. R.W. Todgham).*

corporations when he explained, on the question of disclosure of operating details by CN:

While there is corporate management there remains the answerability and responsibility of the government for the success of the system. That we cannot dispute. But there is no immediate accountability for the day-to-day procedure of operation.¹

Meighen, however, could hardly have supported the view that Parliament can be denied answersto questions on the policies followed by crown corporations, particularly on matters of purchasing, recruitment, expansion, financing, etc..

While crown corporations perhaps lack some of the ingredients of accountability and responsibility normally associated with governmental bodies, theye are by no means immune from political influence and interference. On the positive side, the presidents of both *Eldorado* (ref. Chapter III, page 51) and *Polymer* have acknowledged that a close relationship is maintained between the crown corporations and their respective ministers. *Polymer's* admission occurred during a 1961 Committee on Public Accounts review of the company:

The Chairman: What is the relationship between your company and the government? ... How do you keep the government fully informed?

Mr. Rowzee: ...the government is kept fully informed of our activities through monthly reports giving the sales and all other details of our operation on a month-by-month basis; by our annual report ... by frequent liaison between officials of our department and the Department of Defence Production, such as Mr. Hunter, Mr. Golden, the Minister, Mr. O'Hurley ... the liaison there is very good.²

1. *Canada, House of Commons Debates, 1921, P. 1181*
2. *Standing Committee on Public Accounts, Minutes of Proceedings and Evidence No. 12, May 10, 1961, P. 355*

On the negative side, the experience of *Air Canada* in its efforts to transfer its maintenance facilities from Winnipeg to Montreal is an example of the kind of obstacle that can be faced by a public enterprise. In this particular case, although the airline had received a report from consultants, in 1963, recommending early abandonment of the Winnipeg base and estimating that continued operation "beyond 1966 and through to 1973 would involve the corporation in \$19,800,000 of avoidable expense,"¹ *Air Canada* did not obtain government approval for the transfer of its facilities to Montreal until late in 1968. In the interval, and in fact, even before - as far back as 1957 when the first decision was taken² - the company was subjected to much criticism at the hands of the opposition critics, albeit with a regional bias.

Similar political pressure was applied to *Air Canada* over its decision, again in 1963, to purchase the *Douglas DC-9* aircraft in preference to the *Sud Aviation Caravelle*. After the *Air Canada* board of directors had reviewed the assessment of the airline's technical staff and come to unanimous agreement favouring the DC-9, a political reaction arose in the House of Commons which necessitated a government analysis of the airline's findings. The vulnerability of *Air Canada* to political action is perhaps best illustrated by the following account:

1. Ashley, C.A. & Smails, R.G.H., Canadian Crown Corporations, Macmillan, Toronto, 1965, P. 327.
2. Canada, House of Commons Debates, January 15, 1968, P. 4296

One of the more blatant lobbying campaigns by a foreign government in Ottawa in recent years was that of the French Government which tried to persuade Air Canada to buy the French Caravelle jet. Before Air Canada had reached a decision on what plane to acquire, the French embassy heavily entertained MPs and journalists and attempted to tie Air Canada's choice of jet to the much broader and different question of French-English relations in Canada. They won over several Quebec MPs to this point of view....¹

When, in fact, the issue did flare along racial lines with French-English undertones it was considered serious enough to warrant a statement from the Prime Minister himself:

A thorough review by the government disclosed no reason for directing (Air Canada) to reconsider this decision.²

The statement implies that the management of Air Canada could and would have been over-ruled - as was Eldorado in respect to its exploration program - if the government had considered it necessary. Nor is there any reason to suggest that any other proprietary crown corporation would fare any better if a conflict should arise between the company's commercial activities and the economic, social and political interests of the nation as a whole.

Crown corporations' autonomy is also restricted, in some cases, in pricing policies. The *Farm Credit Corporation* and the *St. Lawrence Seaway Authority*, for example, have been restrained by public policy considerations from raising their charges; several other corporations require amendments to their

1. *Lobbying: Nasty Word or Useful Tool*, *Canadian Business*, July 1969, P. 26.
2. *Canada, House of Commons Debates*, 1963, P. 5051.

acts in order to materially increase their earnings. In a similar vein, *CN* is unable to cease its services to many uneconomic branch lines in the Prairies or the Maritimes without proving its case in detail before the *Canadian Transportation Commission*. Nor, until the advent of ~~jet~~ jet aircraft and the rise of regional air carriers, was *Air Canada* able to significantly reduce its stopping points in low-traffic density centres.

In the area of personnel recruitment crown corporations, for the most part, enjoy the same conditions as do private sector companies. While this is advantageous to management it is not entirely a desirable situation for a public agency since there are no safeguards, such as apply in the civil service, to ensure fair opportunities to all applicants for positions. Nepotism and favouritism can occur in crown corporations on the same basis as in the private sector, since no control agency is charged with scrutinizing recruitment or advancement practices of crown corporations. Nor is there any formal barrier preventing patronage in government companies of the proprietary class. That these abuses are prevented is a tribute more to the ethics, determination and courage of crown corporation managers than to any formal restrictions or external supervision. Latterly, the growth of unions among government companies, which have long been subject to the provisions of the Industrial Relations and Disputes Investigations

Act, has minimized the possibility of choice positions like foremen, supervisors, etc. being available for patronage appointments since such vacancies, under collective agreements, are usually the prerogative of existing staff.

One of the acknowledged strengths of crown corporations has been their ability to compensate their personnel according to industrial wage and fringe benefits standards. Justifying this, C.D. Howe could say:

No one would suggest that the Polymer Corporation, a \$50 million project, with a turnover of \$40 million or \$50 million a year would be operated by a man with a civil service salary.¹

Five years earlier, again referring to Polymer he had argued, in the same context:

The need for a reasonable superannuation and pension plan will be apparent in the case of Polymer alongside the Imperial Oil refinery at Sarnia. The type of employee is much the same as the type of employee of the Imperial Oil refinery ... Imperial Oil has an advanced policy in the matter of superannuation and benefits to its employees. It would hardly be practical for the government to carry on a similar operation alongside without having some plan of a corresponding nature.²

These advantages still exist to a significant degree. The presidents of CN, CBC, possibly Polymer, and the chairman of Air Canada are among the highest paid public employees in the country, earning considerably more than the present \$40,000 ceiling on the salary of the Deputy Minister of Finance, for example. Yet, criticism is being heard from MPs whose own

1. *ibid*, 1951 (Second Session) P. 2176.

2. Canada, House of Commons Debates, May 15, 1946, P. 1515.

salaries are falling behind in the current inflationary period. Robert Stanbury, for instance, writing in the June 1969 edition of *Canadian Business*, pointed to the fact that at least 43 employees of the public service - most of them in crown corporations - earned in excess of \$35,000 per annum in 1968, and that at least 2775 had incomes over \$18,000.¹

However, the amount of latitude available to proprietary crown corporations on salary matters has been somewhat exaggerated. It is true that some corporations, notably *Canadian Overseas Telecommunications Corporation*, *Eldorado*, *Northern Transportation* and *Polymer*, can act to increase the remuneration paid to the chief executive on a vote of the board of directors. Notwithstanding this fact, it must be remembered that the members of the corporations' boards are all appointed by the Governor-in-Council acting on recommendations of the cabinet, and serve on a "during pleasure" basis. Members, therefore, are unlikely to take steps in defiance of expressed government views - in this case, for example, on wage and price restraints - to increase the president's salary and, by that action, the entire management structure. Other crown corporations must obtain orders-in-council to raise the salaries of presidents and vice-presidents, while some require cabinet action on the president alone. In all but a few cases - *Air Canada*, *CBC* and *CN* in particular - the corporations' boards submit recommendations to the ministers responsible,

1. Stanbury, Robert, M.P. - What's an M.P. Worth?, *Canadian Business*, June 1969, P. 60.

thereby at least drawing attention to a need for a salary adjustment. In instances where board advice is replaced by ministerial review, action is likely to be infrequent and very much dependent upon the personality of the individual minister. It is hardly necessary to note that a ceiling on the upward revision of the salary of the chief executives is felt at all levels of management and especially among professional support staff, generally the most mobile employees.

Hence, the assumed strengths of proprietary crown corporations in matters relating to wage and salary administration must be qualified and recognized as not uniform among all *Schedule D* companies. And, in the majority of cases, during an inflationary period, there is more illusion than substance to the autonomy of public enterprise corporations in this area.

Nonetheless, the corporate form continues to offer clear advantages to government in fulfilling certain tasks, particularly state entrepreneurial activities. As such, it would appear to have a continuing role in Canada.

CHAPTER V

THE FUTURE OF GOVERNMENT-OWNED CORPORATIONS IN CANADA

One of the most important developments to occur in respect to Canadian public enterprise in recent years has been the announcement, first in the throne speech of 1963, and later, in subsequent introductory addresses, that a new crown corporation - the *Canada Development Corporation* - would be established. The original intended purpose of CDC was described as follows:

*A measure will be placed before you to establish a Canada development corporation by means of which Canadians can more readily direct their savings to the building of new Canadian industries and to increasing the Canadian ownership of existing industries, which is one of the important objectives of this government.*¹

No legislation was forthcoming, however, and when reference was made to the corporation in 1965, 1966, 1967 and 1968 throne speeches without further action speculation arose as to whether the corporation would ever come into being. In late May 1969, though, legislation was discussed by the Prime Minister who advised a questioner that the subject had "priority" in the government's mind."² Subsequently, later in the same day, the Minister of Finance expressed the hope that the legislation would come before the House before summer recess. He went on to add:

1. *Canada, House of Commons Debates*, 1963, P. 7.
2. *ibid*, 1969, P. 9208.

*I hope that when this corporation is established it will have a role in regard to proposed takeovers of Canadian enterprises. It will be a matter for the directors of the corporation to decide in a particular case whether they wish to invest in a particular corporation ... their judgement will have to take into account the very wide range of complex facts that relate to a particular firm's position and to the Canadian interest in maintaining the Canadian identity of the firm in question. It is not our intention to have the Canada Development Corporation invest in businesses which do not provide a growth potential, in order to call them Canadian.*¹

The Canada Development Corporation has been expected to take over the ownership of three major crown corporations - Canadian Overseas Telecommunications Corporation, Eldorado and Polymer - with the government initially being the only shareholder. Presumably, Eldorado's subsidiaries - Northern Transportation and Eldorado Aviation would also be included. Planning calls for the government to authorize CDC to issue shares to the public early in 1970, or as soon as possible after the legislation is passed - probably this fall - in small enough denominations to permit the small individual investor to buy. Par value of \$5.00 per share has been mentioned.² In some respects, as a holding company with joint public-private ownership, CDC is reminiscent of Italy's IRI, though in a much more embryonic form.

1. *ibid.*, 1969, P. 9224.

2. *Baxter, Clive - CDC Rolling Again - Financial Post, August 17, 1968.*

Much confusion and speculation still surrounds CDC. As originally conceived by Walter Gordon, Minister of Finance in the early year of the Pearson administration, the corporation was to have a primary role in "increasing the Canadian ownership in existing industries". The present approach is not yet clear. A Financial Post editorial noted, a year ago, that there is no way of knowing exact details of how CDC will work until the enacting bill is made public. It went on:

..What is the real philosophy behind CDC? Gordon's original plan ... clearly contained an implication that the corporation would try to "buy Canada back", or at the very least prevent a further sell-out to foreign investors.

Under Sharp, the Ottawa view shifted. CDC became principally a vehicle for transferring crown-owned corporations to the public domain and, almost accidentally, for creating a new capital pool to help finance industrial projects. Sharp did not favour a special seeking-out of the very small investor. The reasoning, and it makes much sense, was that if the government were clearly behind CDC the investor would expect Ottawa to protect his investment for him.

Now, under Edgar Benson, the CDC reappears as an aggressive, profit-oriented organization looking for attractive investment propositions where an infusion of capital and entrepreneurial skill can turn the tide. It will operate on a big scale - probably no investments under \$1 million.¹

There is no indication as to whether CDC will be expected to play a rôle in natural resource development, where large capital investments are imperative, or whether it will - because of small investor expectations - seek to maximize its profits by investing in secondary industrial activity. Nonetheless, the decision to embark on joint public-private

1. Editorial - Risks for the 'Five-Buck' Buyer, Financial Post, August 17, 1968.

investment in a corporate vehicle has opened up new horizons in Canadian public enterprise, even before the *Canada Development Corporation* becomes a reality.

Eldorado, for example, as noted earlier,* has already been authorized to take steps to improve its profitability, presumably to make it a more attractive component of the CDC portfolio. Exploration for a new, economic base metal property - halted by ministerial directive in 1961 - if successful, could inject new potential into the company, generating interest in CDC as a by-product if the expected take-over does materialize. *Polymer* has also significantly improved its profit performance in the past year and has embarked on a major capital investment program to further expand its production and marketing. And *Canadian Overseas Telecommunications Corporation* has just recently reported net earnings for its 1968-69 fiscal year that are 45.2 percent higher than 1967-68's record level, and represent a healthy 11.5 percent return on total investment.**

Although CDC was the first proposed government enterprise in recent memory to raise the issue of co-investment*** delays in its incorporation have denied it the distinction of

* See Page 53.

** The *Canadian Overseas Telecommunications Corporation* 1968-69 Annual Report was received too late to include the results in calculations on pages 66 and 67.

*** The original Trans-Canada Air Lines proposal included provision for participation by Canadian Pacific Railways and Canadian Airways. Both, however, turned down the government's offer of participation.

establishing the precedent. This honour, instead, has gone to *Panarctic Oil Ltd.*, a joint governmental-private sector consortium formed to carry out oil exploration in the Arctic. First disclosed by the Minister of Indian Affairs and Northern Development in an announcement in the House of Commons on December 12, 1967, the consortium consists of twenty Canadian mining companies and the Federal Government, which holds 45 percent of the stock.¹ Although the government has only one directorship on the board - of a total of 14² - the parliamentary secretary to the Minister of Energy, Mines and Resources has revealed that the choice was either "an outright grant .. or to participate", saying that "...the venture on the part of the government and *Panarctic* is an exciting one ... it will produce most important and valuable information regarding what does exist in this part of the world."³

Closer to the *CDC* concept of co-investment, involving small investor holdings, is the most recent joint public-private enterprise creation, *Telesat Canada Ltd.*, which has also lapped the proposed holding company en route to its much-awaited incorporation. *Telesat*, which cleared its first hurdle in receiving Royal Assent for its legislation on June 27, 1969,⁴ is now in process of organization. When introducing the legislation establishing *Telesat Canada*, the Minister of

1. *Canada, House of Commons Debates*, 1967, P. 530
2. *ibid*, 1969, P. 6087.
3. *ibid*, 1969, P. 7565.
4. *ibid*, 1969, P. 10714.

Communications noted that the new corporation would go beyond the precedent set by *Panarctic Oils Ltd.* by:

... combining into a single entity three interests or groups: the government, private industry, which in this case means the common carriers; and the public at large ... I do ... believe that the concept contained within this bill, though not the specific details of the satellite corporation, may serve as a pathfinder for future government-public-private industry partnerships.¹

Later in his presentation he added a further explanation of the relationships of the three parties, noting that each would own a proportion of the corporation which, in turn, would be reflected in representation on the board of directors. He observed also that there would be "...no power without financial responsibility and no responsibility without power."²

One particularly interesting point about *Telesat* is the fact that the corporation begins its operations with clear guidelines as to its profitability objectives. The Minister has insisted that *Telesat* aim for a return of between eight and 12 percent on investment capital initially, setting its own objectives after deciding whether the original range is too low or too high.³ David Golden, formerly Deputy Minister of Industry and, more recently, president of the *Air Industries Association*, has been appointed president of the new corporation.

1. *ibid*, 1969, Pp. 7491-2.

2. *ibid*, 1969, P. 7493.

3. Crane, David, Government Presses for 8-12% Return on Telesat Canada, Globe & Mail, April 23, 1969.

There are some indications that the government's experience with *Panarctic* may lead to further public enterprise developments in the near future. In December, 1968, the Minister of Energy, Mines and Resources was quoted in an article appearing in *Executive Magazine* as having strongly supported the idea of government participation in *Panarctic* then suggesting further public enterprise possibilities in oil development:

In a small country like Canada the government has to be in the oil business to stay competitive ... with the exception of the U.S. all other significant oil producing or consuming nations support at least one company with government participation, Petropar and Aquitaine of France, Royal Dutch Shell, British Petroleum, Mexico's PEMEX and Italy's E.N.I. to name a few.¹

In recent weeks speculation on this subject has emerged, presumably arising out of reports that a special Federal Government task force is now formulating a new petroleum policy. The task force is reported to be studying a crown corporation concept as the vehicle for administering vast federally-held potential oil reserve lands in the north. The government is said to favour entrance into the oil industry for the following reasons:

- It regards the oil industry as perhaps the best available means for opening remote areas. It has proved more effective in bringing industrialization and fat payrolls to certain parts of Canada than any other enterprise. With production established, crude oil and natural gas usually attract other industries to provide assorted services.

1. Neesham, Robin - Energy Minister Joe Greene, *Executive*, December 1968, P. 52.

-The Federal Government has long been envious of large amounts of revenues that now flow to Alberta, for instance, in the form of land fees and other payments. In 1968 Alberta collected almost \$250 million from oil and gas companies. While a crown corporation would not quite benefit from the same revenue sources, its participation in the production end of the oil business would increase federal income from such natural resources.

-The presence of an oil company "owned by all Canadians" in this field is an attractive move to boost nationalistic pride.¹

Yet another development on the subject of crown corporations can be anticipated within the present departmental structure of the government. The Minister of Communications has stated several times that the *Post Office* will be re-organized into a crown corporation, possibly in as early as 18 months. The re-organization itself is, to some degree, now underway but the Minister has indicated that the conversion to corporate status will come only when the *Post Office* has succeeded in eliminating its sizeable annual deficit which approached \$68 million in 1967-68. The criterion for the new crown corporation will be self-sufficiency from mail rate incomes, eliminating, if possible, the need for government mail subsidies.²

Looking to the future of the major profitable crown corporations, one eminent financial columnist has suggested that the Federal Government improve its cash position by selling off, by tender, such entities as *Canadian Overseas*

1. Federally-owned Oil Company Reported Under Study, *Globe & Mail*, September 5, 1969.
2. Tierney, Ben - Kierans Will Make Post Office Pay, *Ottawa Citizen*, August 8, 1969.

Telecommunications Corporation, Eldorado, Polymer and possibly *Air Canada*.¹ The apparent present foetal condition of the *Canada Development Corporation* offers a more attractive alternative: a substantial improvement in the government's cash position while retaining, through government-private capital investment the public ownership character of a select group of attractive, thoroughly Canadian corporations.

In this context, there can be little doubt that Canadian public enterprise - with the recognition of the merits of joint public-private ownership - has embarked on a new and potentially exciting period of development and growth. The establishment of the *Canada Development Corporation* and the incorporation of *Panarctic Oil Ltd.* and *Telesat Canada Ltd.* have charted a new course for experience in government enterprise in Canada which should encourage wider public interest in this important field of government involvement.

1. Meyer, John - If Ottawa Needs Cash - Sell The Crown Corporations, *Monetary Times*, November 1968, P. 13.

CHAPTER VI

SOME SUGGESTIONS FOR IMPROVING THE PERFORMANCE OF GOVERNMENT CORPORATIONS

While it is acknowledged that proprietary crown corporations are, in most cases, well adapted to fulfilling the tasks expected of them, a number of steps might be taken to improve the performance of several of the companies considered in this study without significantly altering the present characteristics of the group.

In a general sense, the cabinet should recognize, in recommending Governor-in-Council appointments to boards of directors of some government companies, that the purpose of such positions - aside from keeping a watchful eye on the management of the corporation on behalf of the shareholder - is to give counsel, based on good judgement and experience, to the full-time management of the company. This has been the case, to a very large degree, in the private sector and has proven to be extremely beneficial. Hence, appointments of directors lacking relevant qualifications should be avoided, except in the case of the *Canadian Broadcasting Corporation*, where directors are expected to be representative of the general public.

The presence of senior civil servants on the boards of directors of proprietary crown corporations has been criticized by many authors, on grounds that they are called

upon to serve two masters.¹ However, the presence of the Deputy Minister of Finance on the boards of specialized financial corporations such as *Canada Deposit Insurance Corporation*, *Export Credits Insurance Corporation*, *Farm Credit Corporation*, and *Central Mortgage & Housing Corporation* would seem to be particularly beneficial in view of the expertise and counsel that he could offer, especially on matters such as the likely availability of new borrowing requirements, expected changes in interest levels, etc.. Generally, however, the placing of a deputy minister on the board of a government company appears to involve duplication since - in most crown corporations - chief executives are at the same level as a deputy minister and both may, in fact, be reporting to the same minister. In such cases, appointment of an outside director would seem to be more appropriate, thus preserving the deputy's independence in offering advice to the minister on matters relating to the corporation, should it be requested.

As noted before, there are presently no safeguards in the form of cabinet directives, control agencies or other supervisory functions which serve to ensure that abuses in personnel recruitment do not occur in crown corporations. A cabinet directive, setting out guidelines to be followed by crown corporations in the selection and promotion of employees,

1. *Hodgetts, J.E. - The Public Corporation in Canada, included in Friedmann, W. (ed.) - The Public Corporation, Carswell & Co., Toronto, 1954, P. 762*

might usefully remind government companies of their responsibilities without unduly complicating their desirable freedom in personnel policies.

A similar approach, could also be taken in respect to purchasing practices of crown corporations in order to minimize the possibility of any favouritism in purchasing and to encourage tendering along accepted public service standards by those few crown corporations that follow traditional private sector procedures. In this latter instance, compliance with uniform standards in purchasing may eventually evolve out of the most recent Economic Council Report on Competition Policy, if the government decides to accept the recommendations contained therein. The report, making particular reference to government companies notes:

Unless a federally-owned enterprise has been specifically charged by Parliament to act otherwise, its use of practices such as refusal to deal or discriminatory buying (for instance, giving arbitrary preference to domestic suppliers) should be subjected to the same tests in respect of efficiency as those appropriate for private enterprises.¹

Proprietary crown corporations - with the exception of the CBC, CN, Farm Credit Corporation and the Seaway Authority - generally receive sufficient funds to avoid the necessity of obtaining appropriations. Two of these can be excluded: the CBC, which has socio-cultural objectives assigned to it by

1. Economic Council, Interim Report on Competition Policy, Queen's Printer, Ottawa, 1969, P. 172.

Parliament making it impossible to be self-sufficient under present circumstances, and *Farm Credit Corporation*, which has, within the past year, been allowed to increase interest rate charges on its mortgages with a view to eventually emerging from a continuing deficit position. In the case of both *CN* and the *Seaway Authority*, however, the future appears bleak unless some remedial action is taken.

There are, in fact, surprising similarities between the two transportation entities: both began operations with large interest-bearing debt obligations and were unable to meet current interest payments, thus plunging even further into debt; both have the Government of Canada as their major creditor; both have had to increase borrowings for expansion and modernization purposes and, in each case, good operating profits are quickly turned into substantial annual deficits, making both appear to have been poor public investments on the part of the government. Yet, there is evidence to support the view that the two entities have each made very significant contributions to economic development in Canada and, as such, were entirely justifiable undertakings by the Federal Government.

The major problem, of course, has been the form of financing employed. Interest bearing debt of substantial proportions is undesirable for a transportation investment since repayment schedules usually assume a fairly rapid increase

in traffic with correspondingly improved earnings. Unfortunately transportation systems do not often shift quickly to the use of a new mode. The build-up tends to be far more gradual than dramatic and the result for *CN* and the *Seaway Authority* - despite each having eventually lived up to its expectations - was a crippling debt which promises to be a drain on the resources of each entity for many decades to come.

In the case of the *Seaway Authority*, the Federal Government is the sole creditor; there is no contributed share capital. Every profit that the *Authority* makes must be directed towards repaying the government for interest expenses on its borrowings. Insufficient payment results in an automatic increase in debt and a corresponding increase in annual interest requirements. If, rather than have had to depend on borrowings, the *Authority* had been established with share capital up to a level of, perhaps, one-half of its financial requirements for construction of the Seaway, with the balance in non-cumulative preferred stock, the total net income could still have been surrendered to the government but interest expense would not have been permitted to accumulate.

The problem, unfortunately, is much more complex. The *Authority* is bound by an international agreement to repay capital and interest on construction out of net earnings after operations and maintenance expenses have been met. The timetable it must adhere to is identical to that of its American

counterpart. Debt accumulation, therefore, ensures that the system is unsubsidized in its operation. A substantial tolls increase would seem to offer a partial solution but unless traffic can be attracted beyond original expectations, and income can be increased at a proportionally faster rate than operating expenses, some form of refinancing will be necessary, if only to avoid an unwarranted charge against some future generation.

CN, on the other hand, as noted in Chapter III, received refinancing up to 50 percent of its indebtedness in 1952. Even this was opposed by its competitors, the *Canadian Pacific Railway* which expressed fear that CN's earnings on the basis of the proposed capital structure would give rise to demands for lower freight rates which, if acceded to, would endanger the future of CPR.¹ The likelihood of a write-off of a large portion of CN's debt at this time appears remote; as a consequence the company's financial plight will undoubtedly continue to worsen.

Although it is unlikely that much can be done to rectify the financial difficulties of either CN or the *Authority* at this time, without disrupting the federal budget, some lessons can be learned from their experiences. Hopefully, as a result, capitalization of such large-scale undertakings will be much

1. Report of the Royal Commission on Transportation, Queen's Printer, Ottawa, 1951, P. 193.

more heavily based on share capital than on borrowings. Also, the international agreement to which the *Authority* is committed, in providing for tolls reviews at five year intervals, weakens its position insofar as it is thus unable to pass on increased costs to customers until the stipulated anniversary date.

Abandonment of this restriction would seem to be essential if any relief is to be obtained over the long term through tolls charges.

The advantage of the corporate form of organization in the private sector is that it provides for certain standards of measurement by which to gauge the performance of a company and, by inference, its management. This is an impossibility at present for several of the proprietary crown corporations examined in this study since the costs of public service obligations have not been separated from otherwise compensatory functions. Yet, accounting techniques permit such segregation and at least two of the non-compensatory corporations do separate the costs of unprofitable or uncharged services from their other accounts.* It would appear, therefore, that such a policy could be followed by *Air Canada* and *Export Credits Insurance Corporation* in cases where services are provided below cost at the request of the government. Isolating these

* *Farm Credit Corporation* isolates revenues from machinery loans, which are compensatory, from mortgages which - at present - are not. The *St. Lawrence Seaway Authority* isolates, for purposes of appropriations, the expenses it incurs from operating non-toll canals.

costs and billing the government for the actual expense, including overhead, would permit examination of the true profitability of the corporation and allow some assessment of the manner in which the corporations' assets have been employed by their respective managements.

Profitability can be a goal of the public corporation if it is applied to those elements of a government firm's activities which may be provided at a profit. In the cases of *Polymer*, *Eldorado* and *Canadian Overseas Telecommunications Corporation* the practice of operating profitably is ingrained in the companies and will be further re-inforced when they are absorbed into the *Canada Development Corporation* where earnings may be expected to be closely watched both by the management of the holding company and by individual investors. *Air Canada* is obviously in the process of evolving into a more profitable operation, if only to meet the expected debt service costs of its new aircraft in the foreseeable future.

In the case of *Export Credits Insurance Corporation*, there is no apparent reason why the company should not be able to set its premiums and interest charges high enough to produce a return on investment comparable to the yield on long term Federal Government bonds. If it is impossible to levy increased charges against all exports insured or financed by the corporation, separate accounts should be maintained. In such situations, if necessary, a subsidy can be claimed on behalf

of those exports that would otherwise lose a marginal competitive advantage in their intended markets. Other, less sensitive goods, however, should be expected to pay the required rate to produce a profit for ECIC.

The *Farm Credit Corporation*, however, is a special problem insofar as it has been required by Parliament to provide low-cost mortgages to farmers and - even if not burdened by the weight of accumulated deficits built up during the years when the corporation had to make such loans at the statutory five percent level - is presently only able to charge one percent above the rate at which it borrows from the government. To break even under such circumstances would mean that the full interest cost on the Federal Government borrowings had been met and that the provision of low-cost mortgages to farmers had been discharged without cost to the taxpayer. This, therefore, should be the goal of the corporation. If, on the other hand, a break-even result is unattainable it would only be equitable to require that the deficit be recovered through annual appropriations, thus drawing the attention of Parliament to the subsidy necessitated by the interest rate ceiling. To merely accumulate deficits, as was done in the past is tantamount to concealment - not on the part of the corporation - but of the minister responsible.

The requirement to perform profitably implies that crown corporations should be free to do so. Hence, if this is

to be an objective, companies like *Eldorado* should not be restrained from taking logical steps - such as diversification - if it is necessary to maintain an acceptable level of earnings.

In this same vein it may be unreasonable to expect the *Canadian Broadcasting Corporation* to increase its advertising revenues at approximately the same rate as its competitors. The type of program that *CBC* feels committed to, under the provisions of the Broadcasting Act, may preclude volume sales of advertising space comparable to private sector broadcasting interests. It is unfortunate that the Act does not indicate the views of Parliament in regard to advertising revenues and the extent to which the corporation should depend on such income. However, there would appear to be no clear reasons for the failure of the *CBC* to act on the recommendations of the Glassco Commission on this subject.

Some consideration might be given, with the objective of improved accountability and responsibility on the part of crown corporations in mind, to the French and British approaches to this subject which are discussed in Chapter I. These represent opposite, yet apparently effective, means of maintaining some measure of control over crown corporations' activities, both in respect to relations with Parliament and with the public. The removal of such relatively independent public enterprise companies as *Canadian Overseas Telecommunications Corporation*, *Eldorado* and *Polymer* from the ranks of fully-owned government corporations,

when - and if - the *Canada Development Corporation* is established, may reduce the problem for Canadian parliamentarians. The other crown companies, mostly Ottawa-based, and having substantial public service orientation - with the exception of *Air Canada* and *CN* - are likely to be more responsive and accountable to Parliament, particularly since most have at least quasi-governmental objects.

Finally, the apparent shifting toward the use of joint public-private investment corporations which has been evolving under Liberal Government administrations since 1963 is an encouraging step. Canada's capital needs, especially for resource exploitation and industrial development are great. The use of the *Canada Development Corporation* and other joint government-private investor companies like *Telesat Canada* and *Panarctic Oils Ltd.*, which may have been patterned after the Italian approach, offers promise of stimulated economic growth, under Canadian ownership. Some lessons from the Italians in respect to the use of holding companies like *IRI* and *ENI* for regional development purposes might prove especially relevant to Canada in meeting the challenge of regional economic development in the quest for national unity.

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