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Linking Regions and Central Governments
Contracts for Regional Development

Chapter 6

The Case of Canada[1]

This chapter examines the use of inter-governmental agreements as contracting mechanisms for Canadian regional development policy. It begins with a review of the decentralisation context, followed by a brief summary of Canadian regional development policy. The chapter then turns to three case studies, each of which describes a different inter-governmental agreement: The Vancouver Urban Development Agreement, The Canada-Manitoba Economic Partnership Agreement, and The Canada-Nova Scotia Gas Tax Transfer Agreement. The analytic framework presented in Chapter 1 is used to assess the "fit" between the co-ordination contexts and contractual arrangements that characterise each of these three agreements.

1. Introduction

In the academic literature on comparative federalism, Canada is generally acknowledged to be one of the most decentralised federations in the world (Watts, 1996). This is the most important factor affecting the character of multi-level governance in Canada as well as the design and conduct of regional policy. This chapter examines how bi-partite and tri-partite intergovernmental agreements designed to enhance regional outcomes can be assessed through the lens of contractual arrangements. It begins with an overview of Canadian federalism before turning to three case studies.

2. Canadian federalism

Canada in 1867 was the first country to combine British-style parliamentary democracy with American-style federalism, though there were centralist mechanisms incorporated into the constitution designed to "resolve" any contradiction which might arise between the contrasting principles of parliamentary supremacy and divided sovereignty. However, these unitary features of the Canadian constitution, such as the powers of reservation and disallowance allowing the central government to block provincial legislation, and the general grant of power given the central government (to maintain peace, order and good government), either fell into disuse or were scaled back through judicial interpretation. Another of these – the declaratory power allowing the federal government to declare any public work to be of national interest and therefore within its jurisdiction – has been used only sparingly (for instance, with regard to nuclear power regulation and facilities). As a result, after a settling-in period Canadian governments, federal and provincial, remained largely confined to and unimpeded in their enumerated fields of jurisdiction as set out primarily in sections 91 and 92 of the 1867 Constitution Act, delimited and protected in this division of powers by court rulings. Until 1949 the external referee was the Judicial Committee of the Privy Council in Britain, and thereafter the Supreme Court of Canada (Simeon and Robinson, 1990).

In terms of the distribution of jurisdictions, foreign policy, defence, and the key economic powers – including control over currency, banks, tariffs, commerce, railways, shipping and, fisheries – were given to the central (federal) government. Agriculture and immigration are concurrent competences. The enumerated powers of the sub-national authorities (provinces) included control over various social, cultural, and education matters, and what were at the time

Table 6.1. **Division of powers between the federal and provincial governments of Canada**

Federal jurisdiction	Provincial jurisdiction
• Sec. 91 – power to ensure Peace, Order and Good Government (general grant of power) • 91.2 – trade and commerce • 91.2A – unemployment insurance • 91.3 – raising money by any mode of taxation • 91.7 – military and defence • 91.10 – navigation and shipping • 91.12 – fisheries • 91.14 – currency • 91.15 – banking • 91.19/20 – interest and legal tender • 91.21 – bankruptcy • 91.22/23 – patents and copyright • 91.24 – Indians and reserves • 91.28 – criminal law • 92.10a – inter-provincial railways, canals, telegraph • 92.10c – works declared to the general advantage of Canada (declaratory power) • 96-101 – appointment and payment of judges • 132 – treaties	• Sec. 92.2 – raising money by direct taxation • 92.5 – public lands • 92.7 – hospitals and health care institutions • 92.8 – municipal institutions • 92.10 – local works (includes roads, bridges, sewers) • 92.13 – property and civil rights (includes social services) • 92.16 – all matters of a local or private nature (general grant of power) • 92A – natural resources • 93 – education
Concurrent with federal paramountcy: • Sec. 95 – agriculture and immigration	Concurrent with provincial paramountcy: • Sec. 94A – pensions

Note: Not a complete listing of respective jurisdictions but a selection of the more significant powers of each level of government.
Source: Canada Constitution Act, 1867.

more immediately local concerns, such as hospitals and asylums, local welfare, roads, municipalities, property and civil rights, and all other matters of a purely local nature. Provinces were also accorded ownership and control over natural resources, a provision that would contribute significantly to provincial fiscal autonomy and to the role of provincial states in economic development. Both levels of government were granted important powers of taxation, though the provinces were limited to direct taxation (for example, property, income, and sales taxes) whereas the federal power to raise revenues was without restriction. Of special note is that the federal government was implicitly granted the prerogative to spend its revenues in whatever manner it chose, without restriction in terms of constitutional field of jurisdiction (Stevenson, 1989).[2]

The use of the federal "spending power", as it came to be known, is crucial to understanding the development of Canadian federalism in the modern (post-war) period. The scope of federal activities and the extent of federal intervention in the national economy and in social affairs increased dramatically during and after the Second World War, especially compared to the highly decentralised federation that describes Canada during the inter-war period. This major shift in government roles and responsibilities was not

accomplished through formal constitutional change: other than an amendment in 1940 transferring unemployment insurance to the federal government, no constitutional change was made in the division of powers. Instead it was the use made of the federal power to raise and spend monies, along with the federal government's embrace of Keynesian economic management policies and techniques (as set out in its 1945 White Paper on Employment and Incomes), that explains this radical change in the respective roles of each level of government. Keynesianism, strong economic growth, and broad public support for the extension and expansion of national social programmes (especially in English-speaking Canada) provided the philosophical and political justification for the centralisation of taxing power and for significant federal spending in the social policy field, even though most of the latter remained formally under provincial jurisdiction (Smiley, 1974).

Initially this centralisation of the Canadian federation was accomplished using tax-rental agreements, whereby the provinces surrendered their taxing power to Ottawa in return for an annual rental payment based on a formula that included an equalisation component. This fiscal arrangement was later replaced by shared-cost, conditional grant programmes, whereby provincial co-operation and participation in nationally-designed programmes was induced through the offer of matching federal funds for the establishment or extension of these programmes. With the phasing out of tax rental agreements, prompted by the refusal of the larger provinces (particularly Quebec) to continue with this practice, a national inter-provincial equalisation scheme was established to address problems of horizontal equity, thereby ensuring the full participation in shared cost programmes of the poorer provinces (Bickerton, 1990). As well, beginning in late 1950s, special bilateral "opt-out" arrangements were negotiated with Quebec, allowing that province to establish its own parallel social programmes in several areas (*e.g.*, higher education, pensions) without financial penalty. This practice of *de facto* differential treatment for Quebec has continued in a rather fitful on-again, off-again manner ever since (Gagnon, 1999).

Over a 20-year period from the mid-1970s to the mid-1990s, federal conditions on financial transfers to the provinces for social programmes were almost completely removed in return for greater certainly regarding the overall size and annual growth in these transfers.[3] This federal concern with the magnitude of inter-governmental transfers extends as well to another important federal-provincial financial arrangement: the equalisation programme. The latter became the centrepiece of Canada's regional policy in the 1960s and remains so today. The fiscal importance and sacrosanct status of these annual bloc payments to less advantaged provinces is reflected in the fact that the principle of making equalisation payments to ensure that provincial governments have sufficient revenues to provide "reasonably comparable levels of public services at reasonably comparable levels of taxation" was included as

Section 36 of the 1982 Constitution Act. The precise formula by which this constitutional obligation has been fulfilled, however, has been altered on several occasions, motivated initially by provincial pressures to make the equalisation formula more comprehensive and later by fiscal pressures on the federal government's ability to fund the transfer created by the province of Alberta's enormous windfall oil revenues (which significantly increased the national average fiscal capacity to which Ottawa was expected to raise all provinces). The equalisation formula, now a middle range five-province standard that excludes Alberta, continues to be the subject of some controversy and disagreement among Canadian governments (Bickerton, 1999; Lazar, 2005). The "special federal advisory commission" has recently delivered a synthesis report on that issue and made recommendations, thus discussions are in process about the implementation of the reforms.

The general discontent that has been registered about the manner in which Canada's horizontal fiscal imbalance has been addressed through the equalisation programme extends as well – with even greater gusto and virtual provincial unanimity – to provincial protestations about a perceived vertical fiscal imbalance between the federal government and the provinces. The nature of this provincial complaint – most vocally and persistently put forward by Quebec – is that a revenue-responsibility imbalance in the Canadian federation has arisen over the past decade that generates large annual budgetary surpluses for the central government. Meanwhile, the provinces continue to struggle to balance their budgets while fulfilling their constitutional and political obligations to provide their residents with costly social services in areas such as health and education. For more precise information on financial relationships between levels of government, see Table 6.2.[4]

Table 6.2. **Federal-provincial division of revenue, expenditures, and inter-governmental transfers**

Central government share of total revenue and expenditures	% of revenue(before transfers): 44 % of expenditure(after transfers): 37
Provincial and local shares of total revenue and expenditures	% of revenue: 56 % of expenditure: 63
CG conditional grants as % of total revenue transfers	43.6% in 1996 (4.3% if transfers for health, education and social services considered unconditional*)
CG transfers as % of provincial and local revenues	19.8% in 1996 (only 0.9% of this conditional if transfers for health, education and social services considered unconditional)
Equalisation transfers (unconditional grants based on formula assessing provincial revenue capacity in terms of 33 revenue sources against a middle-range five-province standard)	42% of all CG transfers (budgetary dependence on this transfer ranges from 30% of provincial revenues to nil; three or four provinces out of ten receive no equalisation transfer)

Note: These transfers are subject to only minimal conditions.
Source: Watts, Ronald (2005), *Autonomy or Dependence: Intergovernmental Financial Relations in Eleven Countries*, IIGR, Queen's University, Working Paper No. 5, Canada.

3. Regional development policy

Besides social transfers and the equalisation programme the federal government has pursued a range of regional development policies since the 1960s. Initially focused primarily on Atlantic Canada and eastern Quebec, in the 1970s the geographic coverage of these regional development policies expanded to include virtually all regions of the country experiencing some form of regional economic disparity.[5] In any event, regional development transfers to provinces as a percentage of total federal spending declined between the 1970s and 1990s, indicating a more modest federal "fiscal effort" in the field of regional development than during the policy's early period (Savoie, 1992; 1997). Indeed, if considered strictly in terms of federal transfers to the provinces explicitly earmarked for regional and industrial development, by the late 1990s these represented only 1% of total federal transfers to the provinces, a miniscule 0.2% of total federal spending, and an even smaller 0.16% of provincial revenues (Vaillançourt, 2000, pp. 200, 210-211).

As well, federal structures and programming in the regional development field have changed quite frequently over the past 40 years. In general these changes moved away from an approach that featured centralised bureaucratic control over the distribution of grants, subsidies, and tax concessions to large manufacturing firms, toward joint federal-provincial funding of a wide and fairly indiscriminate range of projects (though infrastructure, especially transportation infrastructure, has always remained important). Finally, in more recent times, regional development programmes have been delivered by decentralised federal regional development agencies (such as the Atlantic Canada Opportunities Agency and Western Economic Diversification), which play the role of integrating federal action and co-ordination at the regional level. Diverse regions and types of problems can thus be addressed by specific contracts, devoted to specific regional concerns. For the most part these agencies provide relatively modest and indirect forms of assistance (*e.g.*, for training, technology transfer, or market research). This form of economic development assistance, often given in collaboration with other governmental and/or non-governmental partners, is most often directed to small- to-medium sized, region-based enterprises, as well as non-profit organisations or institutions, which compete for available funds based on the innovative character and general worthiness of their proposed projects, whether in the service sector, manufacturing, or research-based activities. This general shift in focus has not precluded, however, the occasional large infusion of development assistance in order to "facilitate" a major investment decision by a multi-national corporation (Bickerton, 1990; Savoie, 1992, 1997). In addition it is worth mentioning the existence of other federal programmes linked to

infrastructures for regional development that support partnerships among levels of government, such as the "Municipal Rural Infrastructure Fund" and the "Canadian Strategic Infrastructure Fund".

While direct federal spending for regional development purposes – as opposed to federal transfers to provinces for same (see above), or the traditional federal roles in economic stabilisation and maintaining an investment climate conducive to growth – has often been important, especially in less-developed regions like Atlantic Canada, it is (and has been) the provinces which have been the primary governmental initiators, planners, and regulators of their own economic development, though often in partnership or with some participation by the federal government. As already indicated, this key economic role for the provinces stems from a number of sources, including their extensive control over natural resources (an important source of economic growth and development in Canada), their constitutional responsibilities for social policy and infrastructure, their undisputed control over municipalities, and their considerable taxation, spending and regulatory powers. In short, with well-established legal claims and political prerogatives, and significant fiscal, policy making and implementation capacities, Canadian provinces have been major economic actors in their own right, while their active co-operation and/or direct participation in federal initiatives is usually considered to be necessary, if not indispensable.

4. Case studies

An assortment of contractual agreements have been used in Canada to achieve regional economic development goals in different co-ordination contexts, using grants, fiscal and/or policy decentralisation, and multi-level collaboration initiatives. Three types of agreements will be presented here. Two of these are related to the Government of Canada's recent focus on urban development. As municipal institutions are fully within provincial jurisdiction in Canada, they traditionally have been ignored in federal policy making in favour of a two-level mode of inter-governmental relations. In the new global economy, however, cities have become critical to the economic health and competitiveness of their national-states, just as Canadian cities in their infrastructure and governance are showing signs of strain. In this connection, a recent OECD study described Canada's "disjointed approach" to urban policy and a lagging national engagement with the problems of cities (OECD, 2002, p. 159).

The primary problem confronting cities in the Canadian system is a mismatch between municipal responsibilities and the policy tools and resources that are available to municipalities. Research institutes and advocacy coalitions in Canada have pressed for improvements in this situation. In 2003, the Government of Canada (GOC) responded with its "New

Deal for Cities and Communities (NDCC)", in essence a group of initiatives featuring a collaborative, multi-level governance approach to the problems of Canada's cities. The NDCC policy had three priorities: to bring an urban lens to federal and provincial policy development, to create administrative machinery for tri-level interaction, and to negotiate revenue-sharing formulas that would channel more federal and provincial tax revenues to municipalities (Bradford, 2004). Urban development agreements were one tool for achieving the priorities set forth in the NDCC (Bradford, 2006). The first case to be examined here is the implementation of a tripartite urban development agreement (UDA), customised to address the particular problems of the targeted city. While a number of these agreements have been put in place in western Canada, it is the first Vancouver Agreement (VA), covering the period 2000-2005, that will comprise the case study.

The second case study is a more conventional, bipartite (national and sub-national) economic development agreement, of the sort that has been used for more than 30 years in Canada. The federal government's decision to work in close partnership with provincial governments in this area reflects the latter's constitutional, political and economic importance in the field of regional economic development, a joint responsibility shared by the two senior levels of government based on their respective economic, social, and regulatory powers and responsibilities. While prior to the 1960s the federal government tended to limit its economic role to international trade, national infrastructure, and the broad fiscal and economic framework for economic development, as noted above it has since become more directly involved in the field of regional development policy. The primary instrument of inter-governmental co-operation used to facilitate this federal role has been the bipartite framework agreement (Savoie, 1992).[6]

Today these multi-generational agreements continue. Previously referred to as General Development Agreements, Economic and Regional Development Agreements, and Cooperation Agreements, this history of inter-governmental co-operation has not been without its problems. These have included a tendency for framework agreements to be used to fund a grab-bag of initiatives representing no particular development strategy or focus (or many simultaneously); the duplication of economic development efforts in adjacent sub-national units without any attempt to incorporate a broader regional perspective; the use of federal monies simply to replace or supplement "normal" sub-national government spending; and the funnelling of federal funds into provincial projects with little or no political credit or recognition given for this financial contribution. Each of these criticisms, along with others, has been levelled at the bipartite development agreement approach since its inception in the 1970s (Savoie, 1992).

In western Canada, the current bipartite framework agreements are referred to as Economic Partnership Agreements.[7] The second case study examined here is the CAD 50 million, five-year Canada-Manitoba Economic Partnership Agreement (MEPA), signed in 2003. The MEPA is cost-shared equally between the federal and provincial government, and administered by a two-person federal-provincial management committee, with joint representation from the federal agency Western Economic Diversification (WED) and the Manitoba Department of Intergovernmental Affairs and Trade.

Another federal initiative associated with the "New Deal for Cities" provides the basis for the third case study. In 2005, a tri-partite (national, regional, local) revenue-sharing agreement was implemented, the purpose of which is to transfer to local governments on an annual basis a portion of the federal revenue derived from the national gas tax. This revenue transfer is to be used by local governments for approved projects that enhance environmental and sustainable infrastructure, a shared policy goal that has been frustrated by the vertical revenue-responsibility imbalance affecting all Canadian municipalities. Like the Urban Development Agreements, the Gas Tax Transfer Agreements regulating the revenue transfer are premised on partnering arrangements between federal, provincial and municipal governments. From the federal government's point of view, this facilitates the utilisation of local knowledge and information and fosters better communication with local actors. The usual and expected political resistance to this type of federal "intrusion" into provincial jurisdiction has been eased in this instance by the respectful but vigorous use of the federal spending power, and the building of mutual trust between governments through open dialogue and joint decision making and action (Bradford, 2004). The particular agreement that will be referred to here is the Canada-Nova Scotia Gas Tax Agreement (NSGTA). It is important to note that although the Gas Tax Agreement initiative is a commitment still being honoured, the current government is shifting away from the NDCC and moving forward with other programmes to address city and community issues.

The contractual relationship assumed by governments when they enter into inter-governmental development agreements of the sort described above is influenced by a number of factors related to the problems governments face in co-ordinating their efforts toward achieving shared policy goals, while in the process protecting their respective interests, and that of the publics they represent. This report suggests several criteria that can be used to evaluate inter-governmental co-ordination contexts: knowledge distribution, complexity, inter-dependencies, and credible/enforceable commitments. Each co-ordination context for an inter-governmental delegation agreement (as determined by these criteria) suggests an optimal set of contractual provisions or "solution". This analytical framework will be used to assess the "fit"

between the respective co-ordination contexts and contractual arrangements that characterise the three inter-governmental agreements in question, with a view to making recommendations on possible improvements.

4.1. The Vancouver Urban Development Agreement

The trilateral Urban Development Agreement between the Government of Canada (central level), the Government of British Columbia (regional level) and the City of Vancouver (municipal level) (the Vancouver Agreement or VA), which ran from 2000-2005,[8] won national and international awards for innovative management and for improving transparency, accountability and responsiveness in the public service (VA webpage). The VA was conceived as a collaborative partnership aimed at moving away from traditional silo-based approaches toward a horizontal model of governance. Its initial focus was on the serious and varied problems of a somewhat notorious area of the city of Vancouver (the Downtown Eastside), which had experienced deteriorating economic, social and health conditions in the 1990s.[9] In response, all three levels of government agreed to the idea of an urban development agreement which would provide the framework for building a common understanding of the problems faced by government and with a view to better co-ordinating the efforts of a wide range of government departments and private sector agencies. It was decided that the VA would be guided by four key objectives:

- to revitalize the main commercial corridor in the target area;
- to dismantle the open drug scene;
- to turn problem hotels into contributory hotels; and
- to make the community safer for the most vulnerable.

Taken together, the myriad and entrenched nature of the problems addressed by the VA, the several policy domains in question, and the distribution of government responsibilities within the Canadian constitutional regime, ensured that there would be a wide variety of actors and agencies involved. This made the co-ordination context for the VA extremely complex. Initially at least the whole purpose of the VA was to better manage this complexity by increasing collaboration between governments to enhance service delivery in the Downtown Eastside; there was no new government funding made available. Eventual dedicated funding for the VA (CAD 20 million) was only provided half-way through the life of the agreement. In effect, the VA's primary purpose was to provide the framework for a new model of collaborative governance.

With severe problems of poverty, unemployment, drug addiction, mental illness, homelessness, crime, and public safety at issue, knowledge and information was both widely and unevenly dispersed amongst the various

agents and actors who initially or eventually were party to the VA. In other words, considerable asymmetries of both skill and information were at play. On some of the projects, or aspects of projects linked to the VA, the federal government can be deemed to possess a high level of expertise and information; on other aspects, the provincial or local (city) governments are better positioned in terms of knowledge and expertise; and all three governments recognised the need to engage community-based non-government agencies or actors whose specific skills and information were considered important to the design and implementation of various projects linked to the attainment of the agreement's objectives. Taken as a whole, all governments recognised that their specific expertise and jurisdictional competencies, when applied separately, were failing to solve pressing problems or attain long-term policy objectives. The multiple asymmetries involved correspond to an extremely complex co-ordination situation in that governments agreed to engage in a process of seeking together solutions to problems that individually they lacked the adequate knowledge, information and/or authority to devise or implement. This high degree of complexity (in the number and diversity of variables, as well as jurisdictional complexities) made unilateral or centrally-designed and controlled solutions impossible.

Generally, the degree of inter-dependence in this co-ordination context was high as well: whether within or between specific initiatives, in terms of horizontal inter-dependence amongst the various policy objectives of the VA; vertically in terms of the impact of various federal policies on elements of the local situation, and vice versa in terms of the potential effects of project outcomes on various matters within federal jurisdiction; as well as temporal inter-dependencies in terms of the influence that successful projects could be expected to have on the local reservoir of societal assets, skills, and capacities, which in turn would exert an ongoing influence on public policy making and local outcomes, as well as on the cost/efficiency of further delegations or decentralised initiatives in the future. Recognition of the inevitable and ongoing inter-dependencies involved in this initiative (because of the nature of the problems being addressed and the distribution of authorities) seems to have provided further impetus for launching this experiment in collaborative governance.

The final criteria in the analytical framework for determining the co-ordination context – the credibility and enforceability of commitments – suggests a varied mix of factors and mechanisms at work in the VA. The agreement envisages enforcement of the various contractual commitments and obligations through a variety of means. Negotiated annual updates to the schedule of initiatives and commitments were required. All governments were directed to work within their own jurisdictions and mandates, to use existing authorisation procedures for committing required funds, to abide by

their own internal controls and mechanisms, and accordingly to be held accountable by their own electorates for their performance. To stimulate and monitor collaboration, at least three levels of political and administrative supervision were established: a Policy Committee comprised of the relevant government ministers and mayor (the decisions of which required unanimity), a Management Committee of senior public officials drawn equally from each level of government (operating on a consensus decision-making model), aided in their efforts by a Co-ordination Unit of officials responsible for implementing the agreement, and finally Task Teams with representatives from each level of government, as well as community and business groups, on particular issues (*e.g.*, economic development, training and employment, drug addiction, crime and enforcement, housing, and food availability).[10] Until 2003, governments were required to work within their existing budgets, thus obviating the need for the creation of new reporting, supervision, or accountability structures or procedures. In the above-stated ways the VA envisaged a co-equal management and supervision process with a variety of pre-existing enforcement mechanisms: the institutional context (in terms of the division of powers and responsibilities), retention of individual governmental authorisation procedures, and external political accountability and citizen supervision (through electoral and other political processes).

The contractual solution within the VA to deal with the co-ordination context described above was the type of open, flexible partnering arrangements necessary for contracting parties with complementary assets and powers, operating on the basis of equality, each (or all) of whom cannot know *ex ante* the precise goals of their co-operation, but wish to engage in a long-term collaboration and co-ordination process. This most closely approximates a relational contract, where delegation is replaced by an equal partnership between governments wherein both policy goals and implementation are chosen co-operatively. The primary obligation of the contracting parties in this type of agreement is to respect and work within a negotiation structure, act co-operatively and in good faith to accumulate and share information, and use this information to act in concert to achieve shared policy objectives. Toward these ends, the VA was designed to provide a framework for building communication, policy and social capital networks that would enhance governmental and stakeholder collaboration and the potential for collective innovation, and ideally to externalise over time some of the co-ordination costs.

4.1.1. Assessment and recommendation

The Vancouver Agreement addressed the apparent inability of governments, and government departments acting separately within their own jurisdictions and mandates, to reverse or effectively ameliorate the

worsening economic, social and health problems of a prominent district in the City of Vancouver. As such, it represents an attempt to replace the dominant governance paradigm (the familiar silo-based delivery of public services) with a radically different model based on inter-governmental collaboration and horizontal management. The partnership constructed by the VA was one based on equality of the three participating governments, utilising unanimity and consensus as its decision-making rule. The relational contractual framework constructed was an enabling one, aimed at achieving greater consultation, co-operation, and collaboration almost as an end in itself, with the shared expectation that more effective service delivery and policy solutions would occur as a by-product of this enhanced cooperation and collaboration.

As an experiment with collaborative models of service delivery, the contractual solution represented by the VA appears to have been "well aligned" with the identified problems and the policy objectives given rise to by these problems. It was both an appropriate contractual solution to the co-ordination context with which governments were presented, and for the most part effective with regard to its main purposes. Efficiencies were gained through greater integration of services and co-operation between governments, thus reducing overlap, dysfunction, and duplication of effort. This does not mean the VA was without problems. One of its early goals – community engagement and community capacity-building – appears to offer room for improvement, with unclear guidelines governing community participation. Another problem, not surprisingly, was a lack of clarity about responsibilities and criteria for decision making. Complaints about a heavy workload for middle managers forced to "moonlight manage" the VA "off the side of their desk" perhaps reflects the lack of new or additional resources allocated to the initiative, and this may also explain managerial perceptions that a lack of dedicated funding for the VA (prior to 2003) was a major weakness in the agreement. However, once such funding was secured, it became evident that managers were encouraged to return to a more centralised, less collaborative approach, with more focus on delivering new services than co-ordinating collaborative relationships. Re-channelling dedicated VA funds through existing programme structures in one of the respective jurisdictions would be one way to reduce or avoid this problem (*A Governance Case Study: Profile of the VA*).

That the VA experience was viewed positively by the participating governments is evidenced by the signing of a second generation VA agreement in 2005. Moreover, at senior levels within the federal government there is continued interest in the efficiencies and benefits that tri-partite arrangements such as these can have in addressing complex issues requiring intervention by all three orders of government in Canada.[11] Perhaps the

greatest challenge for governments and their stakeholder partners will be to sustain and institutionalise the new governance paradigm, and to develop standards and performance indicators (which were absent in the VA). This will be needed to further develop the new generic form or "paradigm" of governance represented by the VA, to make possible a "continuous improvement" cycle in the new paradigm, and to fully take advantage and build upon (in policy making and programme implementation terms) the social capital and policy networks created under the VA (WED Canada, *The Vancouver Agreement*).

4.2. The Canada-Manitoba Economic Partnership Agreement

The second case study presents another variation in coordination context. The Canada-Manitoba Economic Partnership Agreement (MEPA) provides financial contributions to projects within two broad categories: "Building Our Economy" and "Sustainable Communities". The second generation MEPA that is the basis of this case study was signed in 2003 and runs until 2008. Due to a change in economic conditions, it differs somewhat in foci and priorities from past generations of similar bi-partite agreements. With Manitoba enjoying a low unemployment rate and satisfactory economic growth in 2003, there was reduced need for immediate or short term results or benefits from a new MEPA. Other factors became more salient in this economic context, in particular a desire to broaden the development focus to include support for institution development of the sort that would contribute to long-term economic productivity and competitiveness (particularly with regard to research and development capacity). Moreover, a political concern informing the agreement was not to run afoul of WTO rules as they relate, for instance, to business subsidies (see Table 6.3).

Accordingly, the design of the second MEPA examined here continues to shift government development efforts further along a continuum that had begun with the first generation MEPA (1998-2003): in general, moving away from an economic development program designed to provide a high degree of targeted, direct and immediate benefit to particular private sector businesses (typical of government assistance in the 1970s and 1980s), toward a programme that also if not primarily seeks to provide more long-term, indirect benefits that contribute to broader, strategic objectives related to economic restructuring and competitiveness (see Table 6.3). As a result, the MEPA is not constructed as a proposal-based programme open to the public, but instead a programme in which MEPA management targets specific categories of applicants or select projects, including both private sector businesses and non-profit, public sector organisations, universities, and research hospitals, the latter increasingly important as centres of research and innovation (see WED, *WEPA, Final Program Evaluation*, Table 5.5).

Table 6.3. **Government programme benefit continuum**

High degree of private benefit	High degree of public benefit
Direct benefit	Indirect benefit
High degree of tangible output	High degree of intangible output
Strict criteria	Non-specific criteria
Checks, balances, controls	Limited checks and controls
Clear indicators of success	Unclear indicators of success
Demonstrated feasibility	Feasibility not always required
Conditions causing shift to direct benefit programmes	Conditions causing shift to indirect benefit programmes
High unemployment and need for job creation	Low unemployment
Need to expand small business creation	Satisfactory economic growth
Slow economic growth	Short term results not essential
Short-term results needed	Institution development a priority
Concern over foreign ownership	Concern about WTO rules
	Lack of concern over foreign ownership

Source: Adapted from WED (Western Economic Diversification Canada) (n.d.), "Western Economic Partnership Agreements (WEPA): Final Program Evaluation", *www.wed-deo.gc.ca*, Figures 5.2 and 5.3.

With both the federal and provincial government having decades of experience with several generations of this type of agreement, asymmetries of policy knowledge between governments is not a major issue. Each government has developed over time a commensurate level of skill and knowledge in this field, and there is a high degree of mutual understanding with respect to roles and appropriate policy instruments. This general situation, however, does not always or equally pertain with regard to information levels at the project level, where the provincial government has an information advantage in that they are closer to the local community and can draw upon the expertise of their sector departments, for example in assessing or developing project proposals. This is countered to a degree by the consensual, co-decision arrangements within the agreement (which go some way towards equalizing decision-making information between governments), and secondly by the fact that on virtually all projects both governments benefit from the validation of individual project proposals provided by the support and financial contributions of community stakeholders. In effect, the knowledge/information situation sometimes produces between governments a relative equality of position with regard to jurisdiction, knowledge and information, and at other times a modest information advantage for the sub-national government.

The medium-term policy objectives of the MEPA – such as supporting the development of research capacities, infrastructure for knowledge industries, and nurturing the workforce skills relevant to this type of industry – are linked to the broader policy objective of enhancing the long-term productivity and competitiveness of the Manitoba economy. In general, the level of complexity involved in attaining these policy goals is high because of the wide range and

interacting character of the variables involved. On a project to project basis (a wide range of which are eligible for support), the level of due diligence exercised by governments, the credibility and track record of community stakeholders and third-party contractors, and the quality of pre-planning processes (better understood and guided as a result of long governmental experience in this policy field) are relevant factors in managing this complexity.

The degree of inter-dependence (whether vertical or horizontal) with regard to the projects supported by MEPA funding is generally low, with economic and social impacts primarily local or provincial. Again, this will vary somewhat on a project to project basis. This low inter-dependence reduces central government concerns about loss of control or authority. Regarding the credibility and enforcement of commitments, a number of factors contribute to what appears to be a generally low level of mutual concern about this: the three decades of experience with bi-partite agreements of this type, the clear limits to each government's financial commitment, the reassurance provided by community stakeholder support and financial participation, mutual confidence in existing government infrastructure for the performance of accounting, reporting, inspecting, and audit functions, and finally the detailed stipulations in the MEPA regulating joint communications with the public (a factor relevant to satisfying the demands and exigencies of each government's ongoing political accountability to citizens).

As with the Vancouver Agreement, the contractual arrangements set out in the MEPA approximate the characteristics of a relational contract. With administration of the agreement delegated to a two-person federal-provincial management committee (jointly responsible for establishing strategic priorities, administrative guidelines for review, assessment, approval, and implementation of projects, and reporting and evaluation processes), the focus is primarily on project selection and implementation, with minimal resources devoted to management, administration, and evaluation of outputs (WED, *WEPA: Final Program Evaluation*, p. 3).[12]

With one of the desired outcomes of the MEPA "institution development" that will make a contribution toward long-term economic productivity, some if not much of the impact of assistance granted under the Agreement necessarily will be intangible. This makes the efficiency of its grant allocations difficult to measure in quantitative terms; regardless, governments have made little attempt to do so. No *ex ante* performance indicators such as targets or benchmarks are included (WED, *WEPA: Final Program Evaluation*). Since the MEPA is not a legally enforceable agreement, it is implemented essentially at the discretion of the partners; moreover, its dispute resolution mechanisms do not involve third parties. However, there is a political mechanism which for both parties acts as a strong disincentive to any breakdown in co-operation:

citizen, voter and interest group preferences and expectations, and following from this pressure on governments to continue with the allocation of public funds to support job creation, economic competitiveness, and various worthy community projects.

4.2.1. Assessment and recommendation

Like the VA, the Canada-Manitoba Economic Partnership Agreement approximates a flexible and enabling relational contract premised on the equal partnership of the parties who agree to co-operate in the determination and pursuit of broad, shared policy objectives. Its design appears to be guided by three factors: recognition of the primary role assumed by the western provinces in finding ways to enhance their own economic and community development, and the responsibility of the federal government (through WED) to provide support for these efforts; the complexity of the co-ordination situation created by the problems associated with this task; and the relative parity (jurisdictionally and financially) of the two parties to the agreement. While the structure and mechanisms employed in the agreement do not accord well with the notion of delegation from central to sub-national authority, they do align well with MEPA's stated purpose of maintaining and further encouraging co-operation between the two governments to jointly define economic development priorities and to reduce overlap and duplication of their efforts to develop and diversify Manitoba's economy.

The contractual solution relies on a number of factors and devices for credibility, enforcement, and controlling exposure to risk: an environment of mutual trust based on decades of accumulated experience, a co-decision form of management, established administrative procedures and institutional mechanisms, community stakeholder participation, and a defined commitment of financial resources. This generally aligns well with the identified problems and co-ordination context. Its streamlined efficiency in terms of minimal administration costs can be criticized, however, for detracting from monitoring and evaluation capability.

Lacking *ex ante* benchmarks, measurable targets or performance indicators, the claimed economic impact and successes of the MEPA – for example, in terms of leveraged investment, job creation, or business start-ups – is rather difficult to assess (WED, *WEPA: Final Program Evaluation*). Moreover, this particular weakness in the Agreement's design could become more problematic in coming years if there continues to be a shift in focus toward support for non-traditional recipients of regional development assistance, linked to the increasingly important objective of enhancing the province's human resources and its infrastructure supporting knowledge industries. Neglecting to develop and implement an adequate feedback and evaluation mechanism

will limit the Agreement's potential to contribute to feedback learning processes, and therefore to further refinement in the effectiveness and efficiency of government programming in this area.

4.3. The Canada-Nova Scotia Gas Tax Transfer Agreement

The third case study features a very different coordination context from both the VA and the MEPA. In 2005, Gas Tax Transfer Agreements between the federal, provincial and municipal governments were implemented, utilizing a new federal transfer, the Gas Tax Fund Transfer Payment Program as its main financial mechanism. Over five years CAD 5 billion will be transferred to the provinces under this programme, which amounts to approximately one-half of the federal revenues collected from its excise tax on gasoline. The Gas Tax Agreements (GTAs) contain a number of contractual provisions with the following aims: to support Canada's environmental sustainability objectives; to provide long-term, stable, and predictable revenues to enable municipal governments to undertake projects to enhance the quantity and quality of environmentally-sustainable municipal infrastructure; to build capacity at the municipal level; to respect provincial jurisdiction over municipalities; and to ensure inter-provincial equity in revenue allocation for the above-stated purposes.

The specific GTA examined here is the five-year Canada-Nova Scotia Gas Tax Agreement (NSGTA). The conditions placed on the federal monies transferred during the period of the agreement – that they be put towards the creation of new municipal infrastructure that meets the guidelines for the programme – has clear implications for the co-ordination context. This new federal transfer has been inserted into an existing fiscal and institutional framework of clear and uncontested provincial control – including tight financial and regulatory oversight – over municipalities, and this is recognised in the Agreement. Moreover, the building of municipal infrastructure is a task which is well rehearsed and understood by provincial and municipal governments, which have a long history of collaboration on such matters. This means that provinces already have well-established guidelines, procedures, norms and expectations for these types of expenditures, with well-developed technical and project management capabilities. However, the federal government is providing 100% of the financing and the amount of funds being made available to sub-national authorities is significant. Moreover, a political commitment has been made to extend this new federal transfer beyond the initial five-year period, even possibly to make it permanent.

In this co-ordination context, the federal government is subject to asymmetries of both knowledge and information that benefit the other levels of government. This creates the possibility that both adverse selection (hidden information) and moral hazard (hidden action) may occur. Under these

circumstances, in the absence of compensating contractual mechanisms, the probability of central government loss of control over its decentralised fiscal resources is high. On the other hand, the level of complexity involved in the projects funded under the agreement – primarily the building of infrastructure – is relatively low, creating the conditions for observable, measurable, and comparable outcomes. As well, similar GTAs have been signed with all provinces (thereby producing a repeated strategic game situation), so should it choose to do so, the federal government is in a position to accumulate information and to further refine an incentive scheme to ensure optimal provincial and local behaviour in subsequent agreements.

In terms of the criteria of inter-dependence and irreversibility, there would appear to be little long-term risk involved for the central government in the GTAs. The tasks being delegated are almost wholly within provincial jurisdiction, with few spillover effects likely. Nor does efficient completion of the tasks appear to be dependent upon complementary action on the part of the federal government, short of providing the promised funds. Moreover, at this point at least, the transfer of the new funds to provinces (then on to municipalities) is neither permanent nor irreversible; the GTAs have a five-year time horizon, with the possibility of renewal.

The final criteria describing the co-ordination context is the credibility and enforceability of commitments under the Agreement. This is primarily addressed by a new governance mechanism in the form of an Oversight Partnership Committee (OPC), comprised of representatives of the two senior levels of government (Atlantic Canada Opportunities Agency, section Nova Scotia and the Nova Scotia province), as well as the Nova Scotia Union of Municipalities. The OPC provides senior management of the agreement, with more direct and detailed supervision provided by the existing institutional framework (*i.e.*, the administrative laws and financial controls of the province). As well, external enforcement through political accountability to citizens is particularly relevant in this case for the provincial and municipal levels of government, since municipal infrastructure is (and always has been) within their jurisdiction and purview. This ensures clear public and partisan perceptions and expectations regarding the distribution of functional responsibilities in this area of government activity.

This co-ordination context has allowed for the design of an incomplete transactional contract, and the NSGTA approximates this "solution". Included in the Agreement is an incentives/revelation scheme, as well as supervision, monitor, audit, and sanction mechanisms to avoid *ex post* deviation from contractual obligations. With a knowledge distribution that favours the province and municipalities, and the relatively low level of complexity involved in new increments of municipal infrastructure spending, the contracting governments were able to define *ex ante* the policy objectives to be

reached, the strategies for doing so, and the methods of implementation. The NSGTA includes criteria that will be used to assess, and mechanisms to verify, provincial and municipal performance. This corresponds to the logic of delegation in the principal-agent theory of contracts: decentralisation becomes an instrument that allows the central government to take advantage of the knowledge, information and capacities of regional and local authorities to more efficiently and effectively pursue national policy goals (in this case, the building of new environmentally-sustainable, municipal infrastructure "of the centre").

The list of federal and provincial obligations under the NSGTA addresses the possibility that each of the three levels of government may attempt to divert funds, thus frustrating the policy objective and reducing the efficiency of the decentralisation initiative. Several provisions seek to ensure that no existing transfers or funds being spent on municipal infrastructure are clawed back, cancelled, displaced, or allowed to expire as the result of the new gas tax transfer. Commitments to this effect are made by both senior levels of government, and the province agrees to "enforce all terms and conditions of Funding Agreements in a diligent and timely manner and seek remedies from non-compliant Eligible Recipients [municipalities]", including the enforcement of penalties through Municipal Funding Agreements (NSGTA, Sections 3.1, 3.2). Indeed, the annual allocation of the new monies to municipalities will only be triggered by full compliance with all obligations under the agreement (Section 3). The Agreement also includes a commitment (one of the mandates given the OPC) to develop a methodology for the measurement of incremental spending on municipal infrastructure (Section 1).

Further provisions regarding the credibility and enforceability of commitments are evident in clauses on reporting, auditing, evaluation, default, and remedies, all of which appear to be consistent with the logic of transactional contracts (NSGTA, Sections 7, 8). The province is to submit an annual report to the Government of Canada, and an Outcomes Report to its own public at the end of the five-year agreement. The latter will detail the investments made and include information on the contribution of each investment towards the policy objective of cleaner air, water, and reduced greenhouse gas emissions. The province also agrees to submit to an audit by the Government of Canada (if the latter so requests), share any additional information it accumulates, and participate in a joint federal-provincial evaluation of the Agreement. Should the federal government declare the province of Nova Scotia to be in default of any of its obligations under the agreement, it may suspend or terminate its own obligation to pay funds. The OPC will act as arbiter in the event of a dispute or contentious issue (sections 8.1-8.3).

4.3.1. Assessment and recommendation

The Canada-Nova Scotia Gas Tax Agreement is the most recent of the inter-governmental agreements under consideration, and therefore the most difficult to assess in terms of its actual performance. However, compared to the first two cases examined above, it is much more precise in its objectives, hierarchical in its relationships, and endowed with mechanisms for inciting proper behaviour and the fulfilment of contractual obligations. There are some key differences between the NSGTA and the other agreements which explain this. Perhaps most important of these is the funding mechanism around which the agreement is constructed. The Gas Tax Fund Transfer Payment Program is a significant new federal transfer, slated to grow over time, funded out of the revenues generated by the federal excise tax on gasoline. As the contributor of a significant pool of new funds to the budgetary coffers of sub-national authorities, the central government in this instance is placed in a strong bargaining position *vis-à-vis* those authorities regarding the purposes to which the new monies will be put and the methods by which they will be expended. Secondly, the federal policy objective is that the funds be allocated to local governments (cities and municipalities) for the planning and building of local infrastructure, yet these authorities and functions are clearly and indisputably within provincial jurisdiction, requiring the federal government to secure the agreement and active engagement of the provinces in order to achieve the policy objective. Thirdly, the knowledge, expertise, information and capacity to undertake the tasks set out in the agreement lay primarily with the sub-national authorities, forcing the central government to rely on these authorities to use the delegated fiscal resources efficiently, but in the absence of revelation and incentive mechanisms, creating the possibility that this may not be done.

For these reasons the contractual solutions in the NSGTA align well with the co-ordination problems and policy objective. The NSGTA is a legally binding agreement with financial penalties and ultimately the courts as instruments for ensuring the full observation of commitments. Agreement provisions to check any possible diversion, displacement or misuse of funds, by any of the three levels of government – along with other provisions requiring transparency, submission upon request to a federal audit, and annual progress reports to the public – satisfies the mutual concerns of the parties about the credibility and enforcement of commitments. At present an incomplete contract, the commitment on the part of all parties to develop performance indicators suggests the possibility or even probability of evolution toward a more complete contract with incentives and supervision mechanisms, in line with the suggested solution in the framework proposed in the first chapter of this report (see also Table 6.4). Moreover, the requirement that communities develop integrated community sustainability plans, and the provision of

Table 6.4. **From co-ordination contexts to contractual solutions**

Dimension	Values	Contractual Solution	VA	MEPA	NSGTA
Knowledge/ information distribution	HH	Complete *self-enforced incentives*		X	
	HL	Complete *Arbitrage*			
	LH	Incomplete *Audit*	X	X	X
	LL	Co-decision *Arbitrage*	X		
Complexity	High	Incomplete or Co-decision *Audit/Arbitrage*	X	X	
	Low	Complete *Incentives*			X
Inter-dependencies	High	Co-decision *Arbitrage*	X		
	Low	Incomplete		X	X
Enforcement context	Unitary	*Arbitrage*			
	Unitary – Admin. Court	*Supervision*			
	Federal state	Incomplete *Supervision*	X	X	X

resources through the new transfer to help them carry this out, ensures progress towards greater policy, management and implementation capacity at the local level, one of the federal government's policy objectives in both its environmental and cities agendas. In short, the NSGTA constitutes an excellent example of an inter-governmental agreement that utilises contractual design to optimise the effectiveness of the relationship between all levels of government.

5. Conclusion

The principle of contracting between governments is a useful way for governments to organise their relationships in the most efficient manner given the widely varying circumstances and conditions under which they must co-ordinate their actions and interventions, the jurisdictional divisions that often need to be transcended given the complexity and inter-dependence of policy problems, and the uneven distribution of information, knowledge and capacities between levels of government in each policy sector. These realities of governance in all OECD countries require the development of a range of instruments of inter-governmental co-ordination and collaboration that are negotiated, mutually-acceptable, reliable, and flexible. They also must be consistent with constitutional obligations, democratic norms, and the principles of good governance. When conceived as contracts, these arrangements can be regularised and institutionalised, but also revised, adjusted, and fine-tuned to optimize efficiency and effectiveness.

The key to the usefulness of contracts, and therefore to their widespread use, is the existence of trust between the contracting governments and the mutual benefits derived from contracting. This can be facilitated by various fiscal, legal, organisational, and political mechanisms incorporated into the contracts for these purposes, but also by accumulated experience with the contracting process itself.

In the case of Canada, a decentralised federal system means the central government needs to contract in order to take advantage of the knowledge, information, and capacities (legal, administrative, and fiscal) of the regional and local authorities. Central authorities do this in order to more effectively pursue national policy goals, an objective that requires government actions to be co-ordinated, both in areas of shared jurisdiction (environmental policy, regional development) and in areas of exclusive jurisdiction where complexity requires complementarity of government action. A variety of contractual practices have been shown to be relevant in these circumstances, including bipartite, tri-partite, and revenue transfer agreements. Based on the case studies examined herein, a particularly important consideration regarding these contractual arrangements is the need for flexibility, co-decision, and horizontal collaboration to encourage and manage the process of learning in the increasingly complex policy and co-ordination situations facing governments today.

Notes

1. This chapter draws on the contribution of James Bickerton, Department of Political Science, St. Francis Xavier University.
2. This open-ended federal "spending power" was often disputed by Quebec and periodically by other provinces, and was finally confirmed and clarified by a Supreme Court ruling in the early 1990s.
3. The one significant exception to this trend is the Canada Health Act (1984), which re–imposed conditions on the provinces by which they must abide to continue to receive, without financial penalty, the Canada Health Transfer (the annual federal contribution to provincial health care expenditures).
4. The Conservative federal government elected on 23 January 2006, has promised to enter negotiations with the provinces to address this question.
5. While on a per capita basis, the least economically developed region of the country – the Atlantic provinces – continues to be the biggest recipient of federal regional development aid, this is somewhat misleading in that other programmes, such as industry and technology programmes managed by the federal Department of Industry, have provided extensive support and assistance to businesses and communities in Canada's industrial heartland. Arguably it is the latter (much larger) federal expenditures that are more important in shaping and sustaining Canada's regional economies (Beale, 2000; APEC, 2004).

6. Although all provinces have signed agreements of this sort with the federal government, they have been particularly important for those provinces experiencing lagging growth, high unemployment, and other economic disparities (Savoie, 1992).
7. An evaluation of the first generation of these agreements noted that they have been successful in leveraging additional investment from the private sector, increasing the number of business start-ups, contributing to job creation, and fostering intergovernmental partnership toward the shared policy goal of diversifying the western Canadian economy (WED webpage).
8. A second generation Vancouver Agreement was signed in 2005.
9. In 1997, a public health crisis was declared because of rising HIV infection rates among intravenous drug users in the Downtown Eastside. This stimulated the political response that eventually produced the VA.
10. It is the task teams that identified funding priorities and looked for funding through existing government programmes, private agencies, or foundations, or if necessary (beginning in 2003) dedicated VA funds. Consultation with and the direct participation of community representatives throughout this process is noteworthy in that community engagement was one of the original stated purposes of the VA.
11. Trilateral UDAs have been signed with a number of western Canadian cities. A new UDA has been negotiated for the City of Toronto, and is currently awaiting final approvals prior to signing and implementation.
12. Standard internal administrative controls on the disbursement of public funds continue to be applied to discrete projects which are recipients of assistance under the Economic Partnership Agreement.

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Interviews

Mr. Adam Ostry, Director, Policy and Communications, Cities Secretariat, Transportation and Infrastructure Canada.

Mr. Derryl Millar, Director of Operations for Manitoba, Western Economic Diversification Canada.

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