



March 19, 2007

Dear Mr. Okalik:

Canada's New Government took office just over a year ago committed to practicing a federalism of openness and to restoring fiscal balance in Canada. Our objective was to take a comprehensive approach to funding the health, post-secondary education, social services and infrastructure programs that benefit all Canadians. Budget 2006 reaffirmed this commitment, and launched a dialogue with provincial and territorial governments, experts and Canadians on how to return federal transfers to a principled, predictable and formula-driven basis after two years of one-off deals. Over the past year, you and I have spoken a number of times on this important issue, and your views and perspectives have been very helpful.

Today, the Minister of Finance tabled Budget 2007, which sets out our plan for restoring fiscal balance. It takes into account what we heard, delivers on all our commitments, and marks a fundamental return to fiscal balance in Canada. With this plan, all governments will have principled, predictable and long-term support for their key responsibilities. Canadians expect their governments to work together to improve health, post-secondary education, social services and infrastructure across the country. Canadians will also benefit from further reductions in federal taxes.

Specifically, our plan:

- Delivers stronger, principled and formula-driven Equalization and Territorial Formula Financing programs based on the recommendations of the Expert Panel led by Mr. Al O'Brien. It adopts the O'Brien recommendations to move Equalization to a ten-province standard, a long-standing demand of many provinces. It also ensures fairness by implementing a fiscal capacity cap, so no receiving province ends up with a higher fiscal capacity than a non-receiving province.

The Honourable Paul Okalik
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- Delivers on our specific commitments by going beyond the O'Brien recommendations to respect existing agreements with provinces.
- Delivers on our commitment that provinces receiving Equalization will never receive less than they would have received under a formula that fully excludes natural resource revenues, consistent with a national fiscal capacity cap.
- Puts the Canada Social Transfer on an equal per capita cash basis, starting in 2007-08, to support post-secondary education, social assistance and social services equally in all provinces.
- Commits the Government of Canada to putting the Canada Health Transfer on the same equal per capita cash basis when the existing Canada Health Transfer expires at the end of 2013-14 by spelling out that commitment in legislation now. It also commits to ensuring that no province sees a decline in its cash transfers as this commitment to equal per capita cash is implemented.
- Increases the Canada Social Transfer funding for post-secondary education by \$800 million annually beginning in 2008-09 and indexes that amount by 3% per year afterwards.
- Delivers on our commitment to create additional child care spaces by providing the provinces and territories with \$250 million annually beginning in 2007-08.
- Invests in preparing Canadians for the jobs of the future by providing provinces \$500 million annually for labour market training beginning in 2008-09.
- Commits to a major effort to help rebuild Canada's infrastructure by providing, for the first time, long-term, predictable funding for roads, bridges and other important public works. As part of this commitment, the plan delivers on our commitment to extend the Gas Tax funding to municipalities to 2013-14.

What this means in total is an incremental \$39 billion over the next seven years, ensuring steady annual increases to overall federal support for provinces and territories. Moreover, in 2007-08 alone, federal payments to provinces and territories will grow by over \$6 billion compared to 2006-07, including increases in Equalization and Territorial Formula Financing of \$1.5 billion. But, much more fundamentally, this means that for the first time in decades, provinces and territories can now count on long-term, predictable and substantially growing

federal support for shared priorities including health care, post-secondary education, training and social programs, and the rebuilding of Canada's infrastructure.

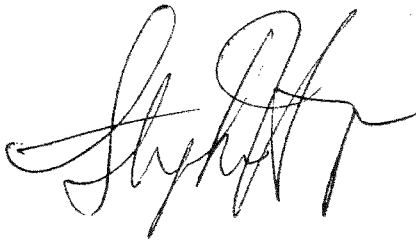
The plan announced today is based on national principles. It treats each province and territory fairly by drawing on the O'Brien recommendations. Our proposals for reforms to Territorial Formula Financing recognize the particular needs of the North, as well as the special needs of Nunavut as identified in the O'Brien Report. Nunavut will also benefit from our formula for allocating infrastructure transfers. This provides all jurisdictions with floor funding of \$25 million per year in recognition of the particular challenges faced by provinces and territories with smaller populations. I listened carefully to your views on these issue, and I am confident that our plan delivers important and lasting benefits to the people of Nunavut.

The Government's plan for restoring fiscal balance establishes a strong foundation based on accountability through clarity of roles and responsibilities, fiscal responsibility and budget transparency, and predictable long-term fiscal arrangements. It provides us with a historic opportunity to launch a new era of collaboration in intergovernmental relations to build a stronger Canada.

Having set a principled framework for fiscal relations, we need now to turn our attention to other key challenges facing the country. As described in *Advantage Canada*, these include ensuring a competitive economic and business environment, developing a skilled, educated and flexible workforce, and ensuring the scientific, environmental and infrastructure foundations for strong, sustainable growth.

I look forward to continue working with you to address the challenges and opportunities we face, building on the solid foundation laid with today's Budget.

Yours sincerely,

A handwritten signature in black ink, appearing to be "Stephen Harper", written in a cursive style.