IS THERE LIFE AFTER DEATH
(OF FEDERAL TRANSFERS)?

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Health Policy Research Unit
Discussion Paper Series
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If there was ever a title of a speech begging for the Mark Twain quip "Reports of my death have been greatly exaggerated," this is it. But it's a little premature. We do not know whether reports of the demise of federal social transfers have been exaggerated, because we have not yet been told how or even whether the new, consolidated federal social transfer, the Canada Health and Social Transfer (CHST), will be indexed.

Without full indexing, the real purchasing power of any cash payment will shrink over time. Even with low inflation of four percent a year, a dollar is worth half as much after only eighteen years. Eighteen years is not a long time for a federal-provincial fiscal arrangement - it is the life span of the Established Programs Financing (EPF) Act that the CHST is replacing. But, even if it shrank in real terms, a cash payment would still retain at least its nominal value. Not so for the CHST.

Each province's CHST entitlement is made up of tax points plus cash. A 'tax point' is a percentage point of the basic federal tax; for example, if a province's income tax is 50 per cent of the basic federal income tax, this is 50 tax points. As part of fiscal negotiations in 1977, the federal government transferred 13.5 personal income tax points and 1 corporate tax point to the provinces. Quebec has a special 'abatement' of additional points due to previous arrangements only it took up. Each year Ottawa will calculate the up-to-date value of the tax points transferred in 1977. Their value increases more or less in line with growth in the economy. This is not part of any fiscal formula, it is just a function of the tax system. The up-dated value of the tax points is then subtracted from CHST entitlements. The result is the amount of real cash paid.

What all this means is that if the value of the tax points goes up more quickly than the entitlements, there is a reduction in cash paid to the provinces. So if CHST entitlements are not fully indexed and do not grow with the economy, the cash payments under the CHST will decrease even in nominal dollars. And they will decrease even faster in terms of real purchasing power.
Failure to fully index the CHST puts it on an accelerated downward escalator, with its nominal payments falling quickly and the real value of its payments collapsing even more rapidly. In the past a partial indexing formula, GNP growth minus three percent, has been used for the EPF. If partial indexing such as this is also applied to the CHST, all federal cash will be eliminated within ten to fifteen years [Battle, 1995]. Because of the special abatement, Quebec would be first to stop receiving any federal cash payments. Next would be provinces with the highest tax point yields, such as Ontario, Alberta and British Columbia. They would soon be followed by all the other provinces.

In light of including tax points as part of the entitlement, we also have to revise our understanding of the fiscal impact of the 1995 Budget. The Budget decreased total provincial entitlements by $4.5 billion from what they otherwise would have been in 1997-98. But the cash paid to the provinces will decrease by a lot more. Cash will be $6.6 billion less in 1997-98 than in 1994-95. In 1994-95 combined Canada Assistance Plan (CAP) and EPF cash payments were $16.9 billion; in 1997-98 cash payments under the CHST will be $10.3 billion [Canada 1995a:51, Table 4.4]. Six point six billion is a headline grabbing figure, but even bigger cuts do not seem to warrant any attention at all if they are made over a sufficiently lengthy period. Partial indexing of the CHST is a one hundred and fifty percent greater cut than the 1995 Budget reductions, it would just take a few years longer.

However, this scenario may not be what is in store for us. Recent signals out of Ottawa are that the cash portion of the CHST will not be allowed to disappear [Globe and Mail, 5 July 1995:4]. Of course, there is a lot of difference between maintaining the cash value of the CHST and not letting it fall to zero. Ten point three billion dollars difference, to be exact. As well, there are rumours that the federal Liberal Caucus is not altogether comfortable with taking on the role of Conservatives in a hurry. Nevertheless, one may safely assume that the Department of Finance will continue its twenty year old campaign to get Ottawa out of social programs and return to the good old days of the 1920s, so nothing should be taken for granted.
There are also many ways to disguise cuts and make partial indexing more palatable or at least more confusing. For example, it might be possible to take advantage of the problem of redistributing the CHST among the provinces to disguise partial indexing. At present the interprovincial distribution of the CHST is unjustifiable, ranging from a low of $840 per capita in Alberta to $1,001 per capita in Quebec [Mendelson, 1995]. There is no possible justification for maintaining the present distribution. This will be one of the topics addressed in the forthcoming federal-provincial discussions. If Ottawa freezes provinces above the highest per capita while fully indexing those below, the result would be a decrease in the total value of the CHST. In short, this would be a tricky way of not fully indexing.

So…it will be some time before we know whether we are indeed looking at the death of federal social transfers. But whether or not they are dead, they are certainly now in the Intensive Care Unit. Let's look at what it will mean if they do not recover.

The obvious consequence - if federal transfers disappear or diminish to insignificance, it will be impossible for the federal government to impose any conditions or national standards on health care and other provincial social programs. The Budget implementation legislation, Bill C-76, gives the federal government the legal right to reduce federal payments other than the CHST in the event of a penalty being warranted under the legislation. However, this is totally unrealistic. Could a future federal government reduce unconditional equalization payments, when some provinces would not be vulnerable at all to such withdrawals? How can national standards be imposed on only parts of a nation? This provision of Bill C-76 should be seen as the smoke screen it is.

Without federally imposed national standards, the single payer medicare system will certainly erode. Some provincial Finance Minister will at some time be unable to resist the lure of saving budgetary expenditures or obtaining additional revenues through this
lucrative source. There are dozens of ways this could be done. Straightforward user fees could be initiated for some services. A private tier, either partially subsidized or unsubsidized, could be permitted. In the favourite of befuddled editorial writers, a special income tax surtax could be imposed on sick people for the value of the services they receive from medicare. For reasons which are obscure, this is often seen as preferable to everyone paying their income tax in the first place. Doctor's extra-billing, which has never disappeared completely, could be legalized again. Creative minds can doubtless think of many other possibilities.

All these alternatives have one thing in common, Canadians end up paying more money for health care, except they have the privilege of not paying it in taxes. Politicians know they can count on a healthy dose of blind anti-tax rhetoric to confuse the issue sufficiently so that most people will never know its costing them more money. Physicians, hospitals and other health care workers would also be tempted by the promise of additional revenue. This creates a ready made constituency of self-interest in favour of the erosion of single payer universal medicare. The more private money there is in the system, the bigger the third party insurers become. They then are an even stronger lobby to maintain and if possible expand their business. As for-profit firms become involved, they will use all the standard advertising and other techniques to drum up business and increase profits.

These are powerful forces. If the dam springs a leak - a small current of payments outside of the single payer system - the precedent will be created and the next, little larger breach will be all the easier. Shoring up the dam is the will of the Canadian people, who overwhelmingly support a single payer health care system but who can all too easily be convinced to tolerate just a little extra out-of-pocket costs, without being aware of the longer term consequences.

Unlike the provinces, the federal government can take a more objective view of the economics of health care, for a very simple reason - they don't have to pay the bills when
the costs go up and they don't have to take the heat of tough choices to keep the costs down. This annoys provincial politicians. But from the perspective of maintaining single payer medicare, it means that at least the federal government is not tempted by the siren song of user charges.

However, we should make no mistake about it. The dam will surely burst if the federal government pulls its finger out. The only question then will be where the system will restabilize. Will we end up with a two tier system like the United Kingdom, with just barely adequate care for most people but luxury care for the rich? Or will we end up like the U.S., with charity for the poor, astonishingly expensive care for those who can get insurance and massive mind-numbing insecurity for middle income families? One way or another, if the federal government allows the CHST to dwindle or even diminish enough that it loses its moral authority, it is the end of universal single payer medicare. It will take some time, maybe decades, so political accountability will only be to history. Nevertheless, this would be quite a legacy for the party that introduced medicare and the Canada Health Act.

All this, however, speaks only to health care services. What about other services? For welfare and personal social services we don't even have to bother waiting for the CHST cash to disappear for national conditions to end. Bill C-76 makes it impossible for the federal government to impose any conditions other than one - that no province will require a residency test. Other than that, there is no place in the law for enforceable national conditions. Section 13(1)(c) of the Act states that one of its purposes is "maintaining national standards where appropriate, in the operation of other social programs," and 13(3) requires the Minister of Human Resources Development to develop shared principles and objectives for these other social programs through mutual consent. But that's all it does. There is no legal basis in Bill C-76 for the enforcement of any conditions other than residency. Even in the extraordinarily unlikely event that conditions were, through some miracle, arrived at by "mutual consent," they cannot be enforced. The
Act will have to be amended to permit enforceable conditions of any kind other than residency [Mendelson, 1995].

It is difficult to conclude other than that section 13 is a decoy put into the Act to mislead social groups, not well known for reading Legislation too carefully. As an extra benefit, it also seems to be misleading the Minister of Human Resources, to whom we can only wish good luck - he'll need it.

The result will be what we are already seeing. The federal government having withdrawn from any protection of those most vulnerable in Canada, has paved the way for a merciless attack on all the programs developed over the last thirty years to provide at least some semblance of a social safety net. The main victims are children, but women and those with disabilities are close behind. In Ontario alone, over half a million children have had their family's subsistence budget for food, clothing and shelter slashed by the provincial government. We can anticipate that the few conditions which existed in the Canada Assistance Plan will soon be violated in many provinces. The social assistance appeal systems in some provinces will be effectively dismantled, and recipients once more will be at the absolute mercy of welfare administrators. So-called workfare will be introduced. All sorts of categorical programs dividing the 'deserving' good poor from the 'undeserving' bad poor will be developed.

The awful truth is that in many respects Canada's last resort social safety net has now become worse than that in the United States. In the U.S., the federal government still maintains some conditionality over welfare programs and there is still a food stamp program. Furthermore, unemployment is lower. U.S. states and the Republican House are only now struggling to obtain unconditional block funding for welfare from the federal government. Unconditional block funding for welfare is exactly what the provinces already got from Ottawa through the CHST.
This might not have much to do with universal medicare, but it certainly will have an impact on the health of the Canadian people. As study after study shows, poverty and ill health are inextricably bound up together. We are right now creating the social problems of the next generation. This, much more than repayments on the public debt, will be the real burden we are passing down to our children. It will be paid in crime, in social disintegration, unlivable neighbourhoods, costly health and social services and a poorly skilled work force.

However, the consequences of the death of federal social transfers are not limited to the inability of the federal government to enforce conditions on provincial social programs. If the $10.3 billion in federal cash payments is allowed to dwindle to a trickle and eventually cease, this will put tremendous fiscal pressure on provincial treasuries. Due to the federal withdrawal of $6.6 billion and the accumulated legacy of debt resulting from the recession and the interest rate policy of the Bank of Canada, most provinces will already be hard pressed over the next decade. For the equalization receiving provinces, there will also be large losses due to the planned cuts in Ontario income tax [Mendelson, 1995]. As a result, the failure to fully index the CHST will mean that all public services - schools, transportation, culture, parks, health care - will be under intense pressure.

There will be economic implications. In a modern economy investment decisions are not made according to who has the lowest taxes. If they were, Germany would not have one of the world's strongest economies. Closer to home, British Columbia would not be enjoying its current prosperity. Rather, factors influencing location of new businesses include a highly skilled work force, proximity to universities and other centres for new ideas and learning, a decent living environment, and reliable transportation, telecommunications and energy infrastructures. This is not to say that business is disinterested in its tax bill. Obviously it is. But this is not the first or the most important factor in the new knowledge economy. What is important is a highly skilled work force, research centres, infrastructure and quality of life.
Unfortunately, it is many of these same qualities which will be worn down and weakened by the demise of federal social transfers. Keeping Canada a prosperous first rank economy requires continued and likely increased social investment. It is just this investment which will be undermined by the end of federal social transfers.

So, is there life after the death of federal transfers? Well, sure there is. People keep going under the most adverse of circumstances. But will it be as good a life as we could have? Will it include universal medicare, a reliable social safety net and increased social investment to produce the next generation ready for the new knowledge economy? It will not.

So to sum up, if there is time, I would like to like to recite a slightly paraphrased version of Antony’s famous speech from Shakespeare’s play *Julius Ceaser*.

**Speech Upon the Death of Federal Social Transfers**

(With Profuse Apologies to W. Shakespeare)

Friends, Canadians, British Columbians, lend me your ears:  
I come to bury federal social transfers, not to praise them.  
The adverse consequences of government programs lives after them,  
the good is oft interned with their bones;  
So let it be with federal transfers. The Finance Minister Paul Martin  
Hath told us federal social transfers were too expensive;  
if it were so, it was a grievous fault;  
And grievously hath federal transfers answer’d for it,  
here, under leave of Paul Martin and the rest of the federal Cabinet, -  
for Paul Martin is an Honourable Privy Councillor;  
so are they all, all Honourable Privy Councillors, -  
Come I to speak in federal transfer payment’s funeral.
They were good transfers, implementing medicare, expanding education and improving social welfare:

But Paul Martin says they were too expensive;

and Paul Martin is an Honourable Privy Councillor.

federal transfers hath brought many provinces to deliver better programs;

whose benefits did the general well-being improve:

did this in federal transfers seem too expensive?

When that poverty hath increased, federal transfers paid more to offset it:

lavish spending should be made of more wasteful stuff:

Yet Paul Martin says they were too expensive;

and Paul Martin is an Honourable Privy Councillor.

You all did see that in the last ten years

federal transfers to provinces as a percent of GDP,

had decreased from 4.5 to 4 percent: was this more expensive?

Yet Paul Martin says they were too expensive;

And, sure, he is an Honourable Privy Councillor.

I speak not to disprove what Paul Martin spoke,

But here I am to speak what I do know.

You all did support federal social transfers once, not without cause:

What cause withholds you then to mourn for them?

O judgement! Thou art fled to TV News,

and Canadians have lost their reason.

Michael Mendelson
September 27, 1995

Notes
1. Equalization receiving provinces will still get equalization cash payments on the tax point transfers; however, these are not related to the social transfer per se.
2. Nurses and organized health care workers have so far been resolute supporters of the single payer universal medicare system. Doctors also turned back a call for user fees at their most recent national meeting. This is contrary to their economic interests, but not to their professional interests.

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