

September 03, 2020



# FEDERAL SUPPORT THROUGH MAJOR TRANSFERS TO PROVINCIAL AND TERRITORIAL GOVERNMENTS



OFFICE OF THE PARLIAMENTARY BUDGET OFFICER  
BUREAU DU DIRECTEUR PARLEMENTAIRE DU BUDGET

The Parliamentary Budget Officer (PBO) supports Parliament by providing economic and financial analysis for the purposes of raising the quality of parliamentary debate and promoting greater budget transparency and accountability.

This report examines federal support through major transfers to provincial and territorial governments over 2008-09 to 2018-19.

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RP-2021-020-s\_e

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# Summary

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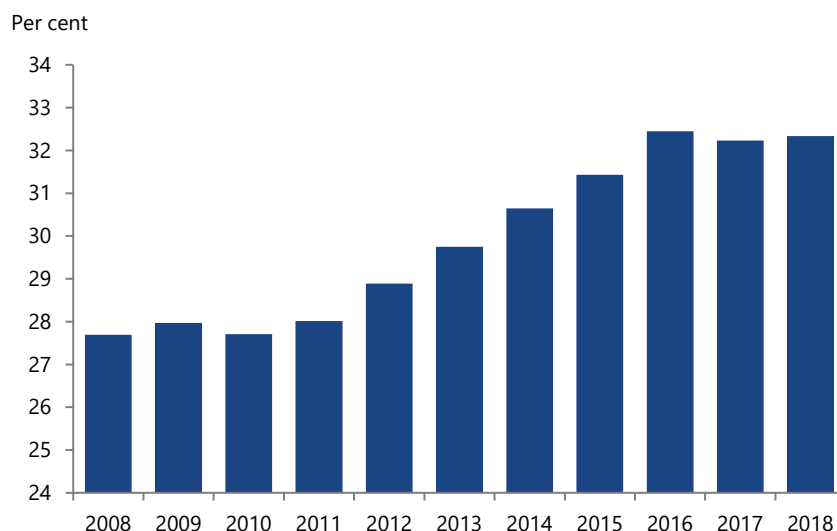
The Canada Health Transfer (CHT) and the Canada Social Transfer (CST) were designed to support provincial and territorial expenses in specific areas. Enshrined in the Constitution, Equalization payments are made to provincial governments to address disparities in their fiscal capacities.

While the structure and formulae used to calculate these transfer payments have evolved over time, there has been over a decade of relative stability. Additionally, higher quality data that ensures consistency across provinces and territories are now available, enhancing the capacity to analyse trends in federal transfers and provincial-territorial spending.

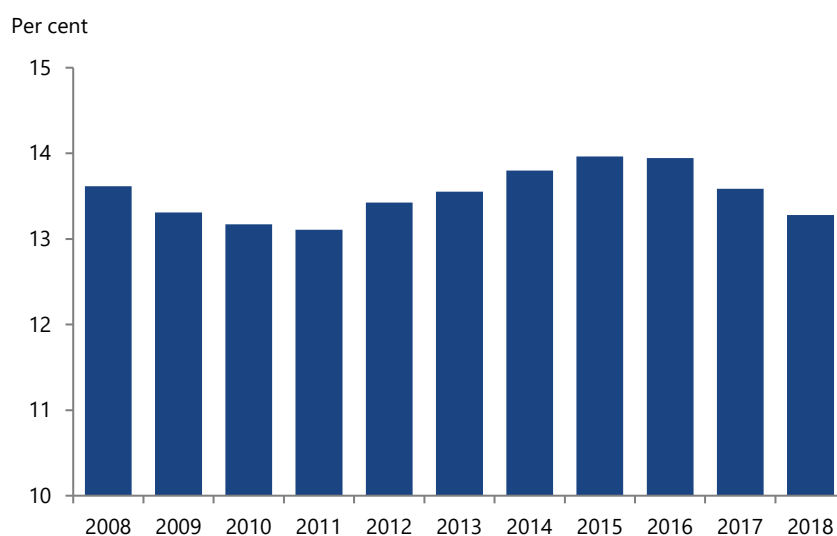
This report examines the relationship between federal CHT and CST transfers, and the provincial-territorial programs for which these transfers were designed, or targeted, to support. In the case of Equalization, this report identifies the federal contribution to equalizing fiscal capacities across provinces, determining whether the program is over- or under-equalizing capacities.

Over 2008-09 to 2018-19, total federal CHT, CST and Equalization transfers increased from \$47.1 billion to \$71.7 billion. At the national level, over the same period, we find that federal support through the CHT increased from 27.7 to 32.3 per cent of provincial-territorial government health spending in CHT-targeted categories. In contrast, federal support through the CST, on balance, edged lower compared to provincial-territorial government spending in CST-targeted categories, from 13.6 to 13.3 per cent.

## Federal CHT payments as a proportion of targeted provincial-territorial health spending



## Federal CST payments as a proportion of targeted provincial-territorial social spending



Sources: Finance Canada, Statistics Canada and Parliamentary Budget Officer.

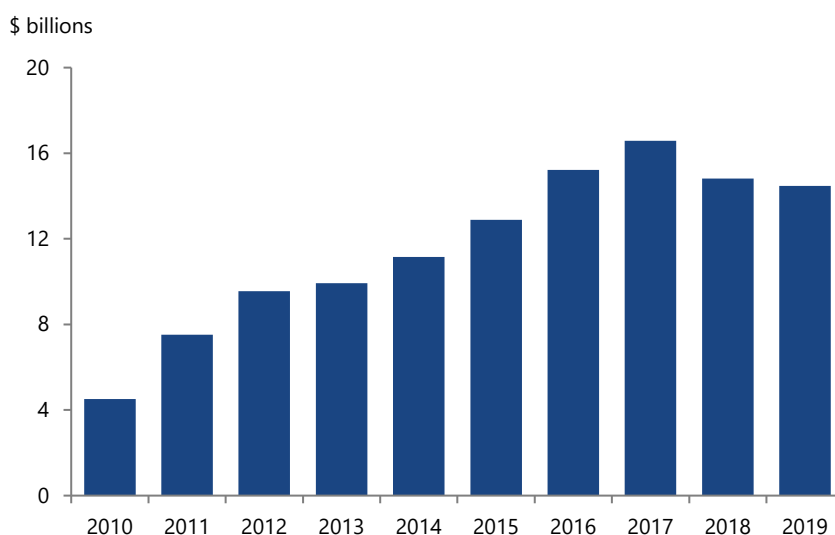
Note: Provincial-territorial expenditures include provincial, territorial, local and aboriginal government sectors. Data are in fiscal years (2008 corresponds to fiscal year 2008-09).

There is, however, considerable variation across provincial-territorial governments both in terms of the magnitude and direction of federal support through the CHT and CST over the period 2008-09 to 2018-19. This variation reflects provincial-territorial government spending decisions and demographic factors, as well as changes to the CHT allocation formula.

- The largest increases in federal CHT support occurred in Alberta and Ontario. Prince Edward Island and the Territories (combined) registered reductions in federal CHT support.
- Most provinces observed a decrease in federal CST support over 2008-09 to 2018-19. Newfoundland and Labrador, Quebec and the Territories (combined) were the only jurisdictions to observe an increase in federal CST support.

In terms of Equalization, our results indicate that, due to the growth rule applied to the overall program envelope (that is, the three-year moving average of nominal GDP growth), the Government under-equalized disparities in fiscal capacities over 2010-11 to 2017-18, resulting in savings of \$16.6 billion over this period.

### Cumulative federal savings in Equalization payments from growth rule



Sources: Finance Canada and Parliamentary Budget Officer.

Note: Data are in fiscal years (2010 corresponds to fiscal year 2010-11).

However, we estimate that in 2018-19 and 2019-20, Equalization payments over-equalized capacities by \$2.1 billion. On a cumulative basis, the Government realized savings of \$14.5 billion over 2010-11 to 2019-20 as a result of applying the growth rule to Equalization payments.

On a cumulative basis, Ontario accounted for \$8.1 billion of the \$14.5 billion in savings resulting from the application of the growth rule to Equalization payments. Quebec was the next largest contributor to the cumulative savings, accounting for \$4.6 billion.

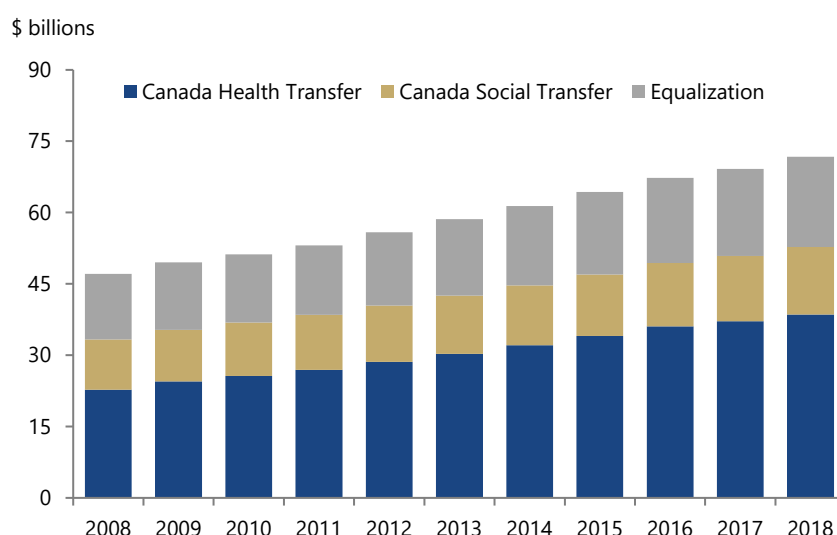
# 1. Introduction

The Canada Health Transfer (CHT), the Canada Social Transfer (CST), and Equalization, are the three largest transfers from the federal government to provincial and territorial governments.

In 2018-19, the CHT amounted to \$38.6 billion, the CST \$14.2 billion, and \$19.0 billion was transferred through Equalization, for a combined total of \$71.7 billion in federal cash payments to provincial and territorial governments.<sup>1</sup> These transfers have increased by 4.3 per cent (2.7 per cent adjusted for inflation) per year, on average, since 2008-09 (Figure 1-1).

**Figure 1-1**

## Major federal transfers to provincial and territorial governments



Source: Finance Canada.

Note: Territorial governments do not receive Equalization payments. Data are in fiscal years (2008 corresponds to fiscal year 2008-09).

Through Alternative Payments for Standing Programs (APSP), transfers to Quebec are reduced to account for prior tax-point transfers (Box 1). All transfers to Quebec in this report are presented on a “gross” basis to ensure consistency with federal transfers to other provinces.



### **Box 1 Federal transfers to Quebec – Alternative Payments for Standing Programs**

Alternative Payments for Standing Programs (APSP) is a tax-point transfer from the federal government to the Quebec government in lieu of a cash payment. Through an arrangement dating back to the 1960s, the federal government reduced personal income taxes by 13.5 percentage points and Quebec increased its personal income taxes by an equivalent amount. Since Quebec collects these revenues through its own income tax system, the equivalent amount is removed from the federal transfers to Quebec (Government of Canada, 2016).

In this report, we include APSP in the calculation of Quebec's Canada Health Transfer and Canada Social Transfer payments. That is, CHT and CST payments to Quebec are presented on a "gross" basis, consistent with the presentation in the Government's budget and updates. Of the 13.5 tax points, 8.5 is allocated to the CHT, and the remaining 5 percentage points to the CST (Courchene, 2008).

APSP combined with the Youth Allowances Recovery (amounting to 3 percentage points) forms the Quebec Abatement, which is shown and calculated on federal personal income tax forms in Quebec.

CHT and CST transfers were designed to support provincial and territorial expenses in specific areas. Enshrined in the Constitution, Equalization payments are made to provincial governments to address disparities in their fiscal capacities.

While the structure and formulae used to calculate these transfer payments have evolved over time, there has been over a decade of relative stability. Additionally, higher quality data that ensures consistency across provinces and territories are now available, enhancing the capacity to analyse trends in federal transfers and provincial-territorial spending.

This combination of high quality, consistent data and a lengthy period of relatively stable program structure, provide a unique opportunity to analyse recent trends in federal transfers and make comparisons of government spending.

Previous reports have typically compared federal transfers such as the CHT or CST to total provincial-territorial spending on health or social services to identify the extent of the Government's support in these areas.<sup>2</sup> However, these transfers were not designed to provide comprehensive support for provincial and territorial spending in these areas.

This report examines the relationship between federal CHT and CST transfers, and the provincial-territorial programs for which these transfers were designed, or targeted, to support. In the case of Equalization, this report



identifies the federal contribution to equalizing fiscal capacities across provinces, determining whether the program is over- or under-equalizing capacities.

The remainder of the report is structured as follows. Section 2 provides an overview of each federal transfer. Section 3 discusses the data and methodology. Section 4 concludes with the results.

## 2. Federal Transfers

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To determine the categories of provincial and territorial spending for which the CHT and CST were designed to support, we relied on the stated objectives of these transfers. In the case of Equalization, we compare the actual payments made to provinces to hypothetical payments that would reduce disparity in fiscal capacities across provinces, consistent with the commitment in the Constitution.

### 2.1. Canada Health Transfer

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There are two key pieces of legislation that we referenced for determining which provincial and territorial government health expenditures the Canada Health Transfer (CHT) was designed to support: 1) the *Canada Health Act* (CHA); and 2) the *Federal-Provincial Fiscal Arrangements Act* (FPFAA).

The CHA explicitly defines the provincial and territorial health services eligible for contributions from the federal government, whereas the FPFAA lays out the calculations of the contributions to health known as the Canada Health Transfer.<sup>3</sup>

The CHT is the funding vehicle through which the federal government supports provinces in their provision of services defined in the *Canada Health Act*.

Since the FPFAA indicates that the CHT is subject to the criteria and conditions outlined in the CHA, we used the CHA criteria as our definition of provincial and territorial health expenditures for which the CHT was targeted to support.

Based on the CHA criteria, we determined that the CHT targeted provincial and territorial government spending on the following categories:

- Hospitals;
- Physicians;
- Nursing home intermediate care services;
- Adult residential care services;
- Services in converted mental hospitals;
- Home care services; and,
- Ambulatory health care services.

CHT funding is fungible; funds can be dispensed as provincial and territorial governments see fit. In this report, we link the CHT to the categories explicitly identified in the CHA as listed above. This is similar to the approach in the

Romanow Report which compared federal contributions through the CHT to provincial and territorial spending on hospitals and physicians (Romanow, 2002). However, we also include 'extended health care services', which were included in the purpose of the *Canada Health Act* (RSC 1985, c. C-6).

Over the period 2008-09 to 2013-14, total CHT cash transfers increased by 6 per cent annually, as committed to under the *10-year Plan to Strengthen Health Care*.<sup>4</sup> The allocation of cash payments across provinces over this period was determined, in part, by the value of federal income tax points in each province (Library of Parliament, 2011). Total CHT (cash) transfers continued to grow at 6 per cent annually until 2016-17, after which their growth rate was reduced to a three-year moving average of growth in nominal gross domestic product (GDP), with a minimum increase of 3 per cent annually.<sup>5</sup>

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## 2.2. Canada Social Transfer

We relied on the *Federal-Provincial Fiscal Arrangements Act* (FPFAA) to determine the list of provincial and territorial government services which the *Canada Social Transfer* (CST) was designed to support.

Based on the FPFAA criteria, we determined that the CST targeted provincial and territorial spending on the following categories:

- Programs in respect of post-secondary education;
- Social assistance and social services;<sup>6</sup>
- Early childhood development; and,
- Early learning and child care services.

The CST is an equal per-capita transfer to provinces and territories. Since 2007-08, the CST has consisted entirely of cash transfers, rather than a combination of tax points and cash, with a legislated annual growth rate of 3 per cent. For five years beginning in 2008-09, there were transitional payments made to provinces and territories to ensure that no province or territory would receive less than they would have under the previous structure.

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## 2.3. Equalization

The objective of the Equalization program is stated in the *Constitution Act, 1982* (Section 36(2)) which commits Parliament and the Government to the principle of making payments to "...ensure that provincial governments have sufficient revenues to provide reasonably comparable levels of public services at reasonably comparable levels of taxation." (Constitution Act, 1867).

In general, Equalization entitlements are based on a province's capacity to generate revenues compared to a standard. If a province has a fiscal capacity below the standard, payments are made to bring that province up to the standard. Provinces with a fiscal capacity above the standard do not receive a payment nor are they required to make contributions to bring their fiscal capacity down to meet the determined standard.

Entitlements are determined using fiscal capacities in a number of categories. For a given category of revenue, fiscal capacity is typically measured as a per capita tax base (for example, personal income per capita).

The formulae for calculating Equalization entitlements and payments have evolved over time. In 2008-09, initial provincial entitlements were calculated using a metric-based standard introduced in Budget 2007. Specifically, the per capita fiscal capacity of each province was compared to a national average.<sup>7</sup> Next, entitlements were adjusted to ensure that no province receiving Equalization would have a higher fiscal capacity (inclusive of the payment) than a province that did not receive Equalization. This adjustment is referred to as the fiscal capacity cap (FCC).

Beginning in 2009-10, the total envelope of Equalization payments was legislated to limit annual increases to a three-year moving average of nominal GDP growth—known as the “growth rule”.

This growth rule was implemented to restrain federal spending on Equalization, and acts as a ceiling.<sup>8</sup> Given this restrictive structure, it could be the case that Equalization payments fall short of entitlements that would bring provinces up to the national average standard, resulting in “under-equalization”.

Conversely if total entitlements fall short of the amount implied by the growth rule, “over-equalization” would occur by adjusting payments upward such that the rule was maintained as required by legislation.

### 3. Data and Methodology

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We use Statistics Canada's Government Finance Statistics (CGFS) and data from the Canadian Institute for Health Information (CIHI) as the basis for our analysis of CHT and CST support. A relatively recent data framework, the CGFS support comparative fiscal analysis by overcoming definitional and accounting differences between public entities. As such, it provides the consistency necessary for a coherent view across all levels of government in Canada.

The Canadian Classification of Functions of Government (CCOFOG) is part of the CGFS and is used to break down government expenditures according to their broad purpose. Thus, CCOFOG offers a benchmark for analysing government contributions toward a specific goal, such social services.

For social spending, we were able to reasonably isolate provincial and territorial expenditures aligned with the objectives of the CST using the CCOFOG. However, the level of detail required to isolate specific health expenditures that align with the objectives of the CHT is not available. Therefore, we opted to use data from CIHI.<sup>9</sup>

Below is an overview of the sources to measure federal contributions and targeted provincial and territorial health and social expenditures:

Expenditure	Data Source
Federal CHT and CST	Open Government – Canada, Department of Finance, Historical Transfer Tables: 1980 to present, Canada Health Transfer (Cash Component), url: <a href="https://open.canada.ca/data/en/dataset/4ee1558-45b7-4484-9336-e692897d393f#wb-auto-6">https://open.canada.ca/data/en/dataset/4ee1558-45b7-4484-9336-e692897d393f#wb-auto-6</a>  Open Government – Canada, Department of Finance, Historical Transfer Tables: 1980 to present, Canada Social Transfer (Cash Component), url: <a href="https://open.canada.ca/data/en/dataset/4ee1558-45b7-4484-9336-e692897d393f#wb-auto-6">https://open.canada.ca/data/en/dataset/4ee1558-45b7-4484-9336-e692897d393f#wb-auto-6</a>
Provincial-territorial health expenditures	Canadian Institute for Health Information by use of funds, age, sex, province
Hospitals	CIHI, NHEX, P/T, Municipal, Social Security Funds Hospital
Physicians	CIHI, NHEX, P/T, Municipal, Social Security Funds Physician
Nursing home intermediate care	CIHI, NHEX, P/T, Municipal, Social Security Funds Other Institution
Adult residential care	CIHI, NHEX, P/T, Municipal, Social Security Funds Other Institution
Converted mental hospitals	CIHI, NHEX, P/T, Municipal, Social Security Funds Hospital
Home care*	CIHI, NHEX, P/T, Municipal, Social Security Funds Other Health Spending
Ambulatory health care	CIHI, NHEX, P/T, Municipal, Social Security Funds Hospital
Provincial-territorial social expenditures	Statistics Canada, Table 10-10-0005-01, Canadian Classification of Functions of Government (CCOFOG) by consolidated government component
College education	CCOFOG 7093
University education	CCOFOG 7094
Sickness and disability	CCOFOG 7101, 7103
Old age	CCOFOG 7102
Social protection not elsewhere classified†	CCOFOG 7108, 7109
Social exclusion	CCOFOG 7107
Early childhood development	CCOFOG 7104
Early learning and child care services**	CCOFOG 7104

Note: \* Spending on home care could not be isolated from other health spending. It was therefore excluded from provincial and territorial health expenditures.<sup>10</sup>

\*\* Early learning child care services were not explicitly listed in CCOFOG, but seemed to be included within 7104.

† 7108 (R&D Social protection not elsewhere classified) could not be separated from 7109 (Social protection not elsewhere classified), and so was included. Together, these classifications represent roughly 2.6 per cent of total provincial-territorial spending on social services (that is, excluding the education portion).

Data from CCOFOG were available from 2008 to 2018. To project to 2019, PBO used the growth rate for the combined education and social expenditures published in the supplementary data with the 2020 Fiscal Sustainability Report (PBO, 2020). Data on health spending from CIHI were used for the period 2008 to 2019.<sup>11</sup>

We used the Department of Finance's numbers for the values of CHT and CST payments to provinces and territories. These amounts are gross amounts and include the APSP.

All data were converted from calendar to fiscal years by multiplying 75 per cent of the current year and adding 25 per cent of the following year. For example, 2008-09 was calculated by multiplying 75 per cent of the 2008 value and adding 25 per cent of the 2009 value.

Data on Equalization payments over the same period (on a fiscal-year basis) was provided by Finance Canada.



## 4. Results

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Over 2008-09 to 2018-19, at the national level, we find that federal support through the CHT increased from 27.7 to 32.3 per cent of provincial-territorial government health spending in CHT-targeted categories. In contrast, federal support through the CST, on balance, edged lower compared to provincial-territorial government spending in CST-targeted categories, from 13.6 to 13.3 per cent.

There is, however, considerable variation across provincial-territorial governments both in terms of the magnitude and direction of federal support through the CHT and CST. This variation reflects provincial-territorial government spending decisions and demographic factors, as well as changes to the CHT allocation formula.

In terms of Equalization, our results indicate that, due to the growth rule applied to the overall program envelope, the Government under-equalized disparities in fiscal capacities over 2010-11 to 2017-18, resulting in a savings of \$16.6 billion over this period. However, we estimate that in 2018-19 and 2019-20, Equalization payments over-equalized capacities by \$2.1 billion. On a cumulative basis over this period, the Government realized savings of \$14.5 billion as a result of applying the growth rule to Equalization payments.

### 4.1. Federal support for CHT-targeted health spending

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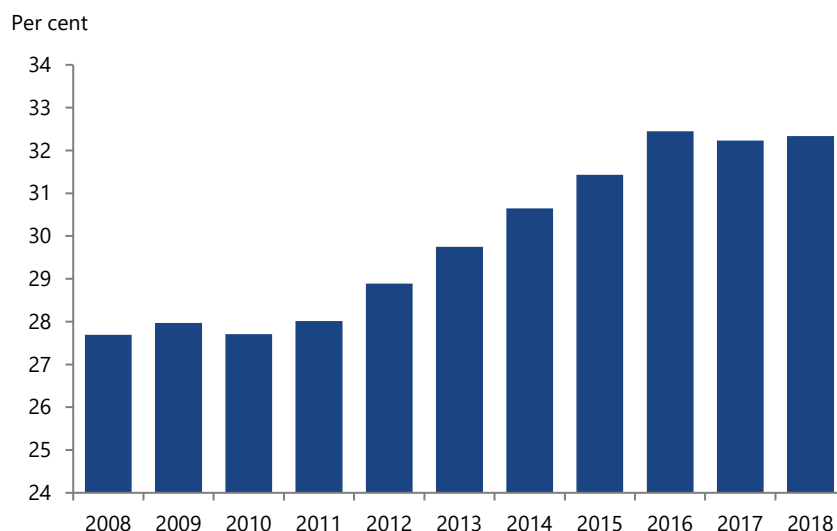
In 2018-19, at the national level, we calculate that the CHT supported \$38.6 billion of \$119.3 billion (32.3 per cent) in provincial-territorial government health spending on CHT-targeted categories.<sup>12</sup>

Federal CHT support remained relatively stable over 2008-09 to 2011-12 at around 27.8 per cent of provincial-territorial health spending (Figure 4-1). Federal support then increased steadily over 2012-13 to 2016-17, rising to 32.4 per cent. Federal support over this period increased as the CHT grew at 6 per cent annually while provincial-territorial governments restrained their spending on hospitals, physicians and other institutions (Figure 4-2). From 2012-13 to 2016-17, provincial-territorial governments limited CHT-targeted health spending growth to 2.9 per cent annually on average—just under half of the growth rate of CHT transfers.

Since 2017-18, the CHT has grown in line with the three-year moving average of nominal GDP, resulting in average growth of 3.4 per cent annually over 2017-18 and 2018-19, and roughly matching the growth in provincial-territorial health spending in CHT-targeted categories.

Figure 4-1

## Federal CHT payments as a proportion of targeted provincial-territorial health spending

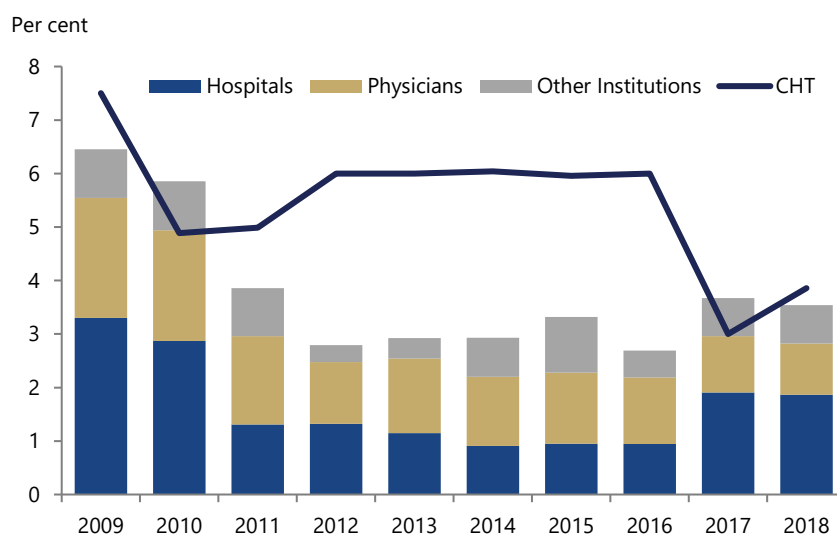


Sources: Finance Canada, Canadian Institute for Health Information and Parliamentary Budget Officer.

Note: Data are in fiscal years (2008 corresponds to fiscal year 2008-09).

Figure 4-2

## Growth in federal CHT payments and targeted provincial-territorial health spending



Sources: Finance Canada, Canadian Institute for Health Information and Parliamentary Budget Officer.

Note: Spending components are shown as contributions to growth. Data are in fiscal years (2009 corresponds to fiscal year 2009-10).

In 2018-19, federal CHT support for provincial government health spending in CHT-targeted categories ranged from 24.6 per cent in Newfoundland and Labrador to 35.5 per cent in Ontario (Figure 4-3). Given the equal per capita allocation of CHT payments, this variation is due to differences in per capita health spending across provinces, which reflect provincial government spending decisions and demographics (Figure 4-4).

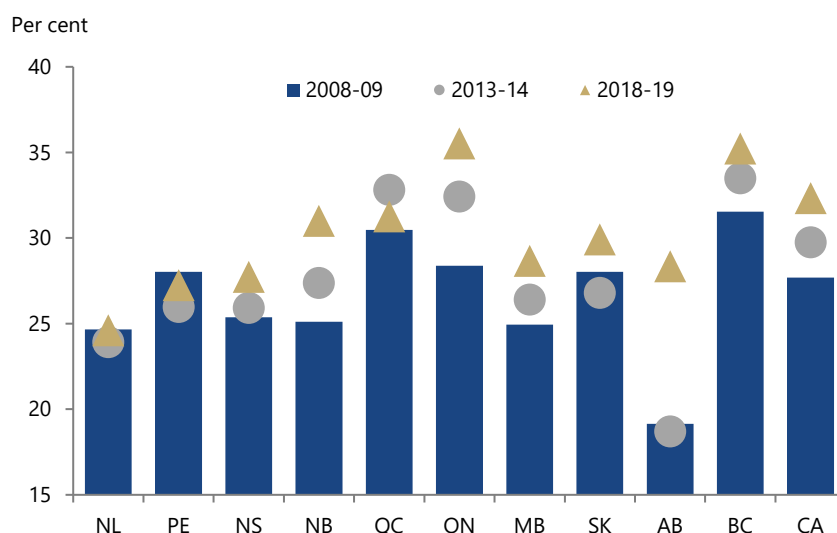
Over the period 2008-09 to 2018-19, most provinces observed an increase in federal CHT support relative to their spending on CHT categories.

The largest increase in federal CHT support occurred in Alberta (9.2 percentage points), with CHT payments growing at 9.6 per cent, while CHT-targeted health spending grew at 5.4 per cent annually, on average, over 2009-10 to 2018-19. The outsized growth in CHT payments to Alberta reflects the transition to the equal per capita cash allocation formula that occurred during this period.

Federal CHT support also increased significantly in Ontario over 2008-09 to 2018-19, rising by 7.1 percentage points of targeted provincial spending. However, this increase was due to restrained growth in provincial government health spending—growth in federal CHT payments averaged 5.2 per cent while growth in provincial CHT-targeted spending averaged 2.9 per cent annually.

Figure 4-3

### CHT as a proportion of targeted provincial-territorial health spending

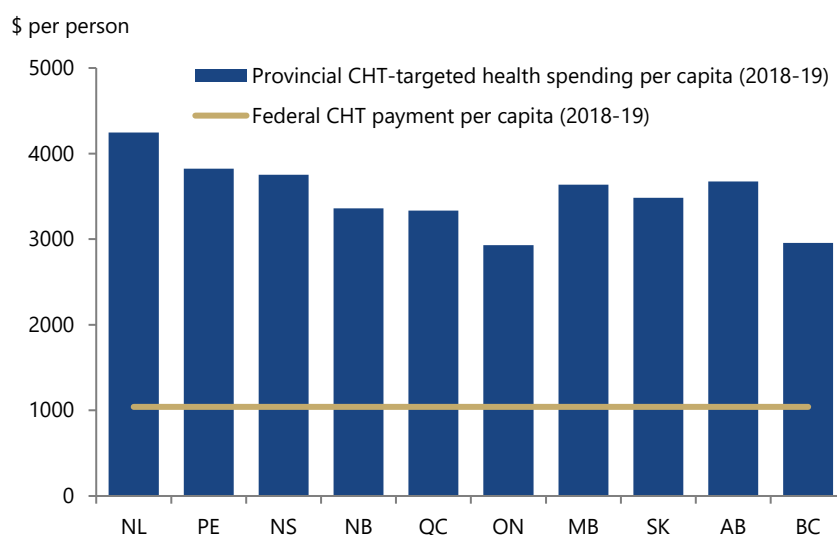


Sources: Canadian Institute for Health Information, Finance Canada and Parliamentary Budget Officer.

Note: For the Territories (combined), CHT support was 15.1 per cent in 2008-09 and 14.8 per cent in both 2013-14 and 2018-19.

Figure 4-4

### Per capita targeted provincial health spending and CHT



Sources: Canadian Institute for Health Information, Statistics Canada, Finance Canada and Parliamentary Budget Officer.

Note: For the Territories (combined), per capita targeted health spending amounted to \$7,050 in 2018-19.

Prince Edward Island was the only province to register a notable reduction in federal CHT support relative to their health spending over 2008-09 to 2018-19.<sup>13</sup> This is explained by its strong growth in CHT-targeted spending—the second highest among provinces, averaging 5.2 per cent annually—combined with below-average growth in CHT payments (4.9 per cent versus 5.4 per cent). The Territories (combined) also saw their federal CHT support decline over this period, from 15.1 per cent in 2008-09 to 14.8 per cent in 2018-19.

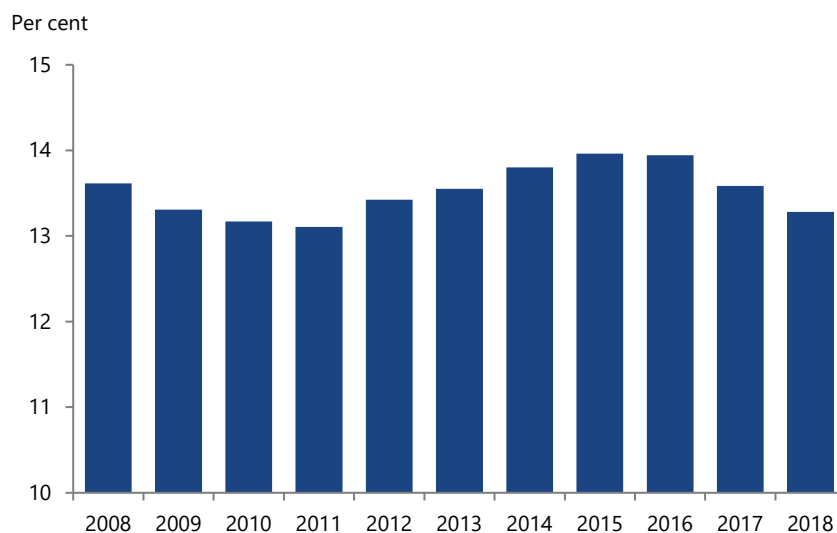
## 4.2. Federal support for CST-targeted social spending

We calculate that the CST supported \$14.2 billion of \$106.6 billion (13.3 per cent) in provincial-territorial government spending on CST-targeted categories in 2018-19.<sup>14</sup>

Federal CST support was 13.6 per cent of provincial-territorial social spending in 2008-09, after which it declined but remained relatively stable, averaging 13.2 per cent over 2009-10 to 2011-12 (Figure 4-5). Federal support then increased steadily, rising to 14.0 per cent in 2015-16 before falling to 13.3 per cent in 2018-19—only 0.3 percentage points below its 2008-09 value.

**Figure 4-5**

### Federal CST payments as a proportion of targeted provincial-territorial social spending

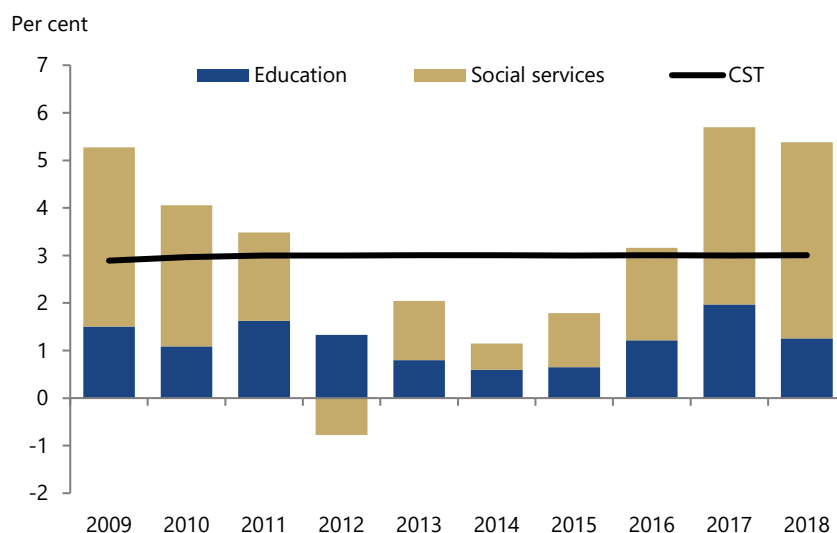


Sources: Finance Canada, Statistics Canada and Parliamentary Budget Officer.

Note: Data are in fiscal years (2008 corresponds to fiscal year 2008-09).

Annual growth in the CST has been set at a rate of 3 per cent since 2007-08. At the same time, provincial-territorial spending on education and social services has grown at 3.2 per cent annually, on average, since 2009-10 (Figure 4-6). From 2012-13 to 2016-17, provincial and territorial governments restrained their spending on education and social services, even reducing the absolute level of their spending on social services in 2012-13.

**Figure 4-6** Growth in federal CST payments and targeted provincial-territorial social spending



Sources: Finance Canada, Statistics Canada and Parliamentary Budget Officer.

Note: Spending components are shown as contributions to growth. Data are in fiscal years (2009 corresponds to fiscal year 2009-10).

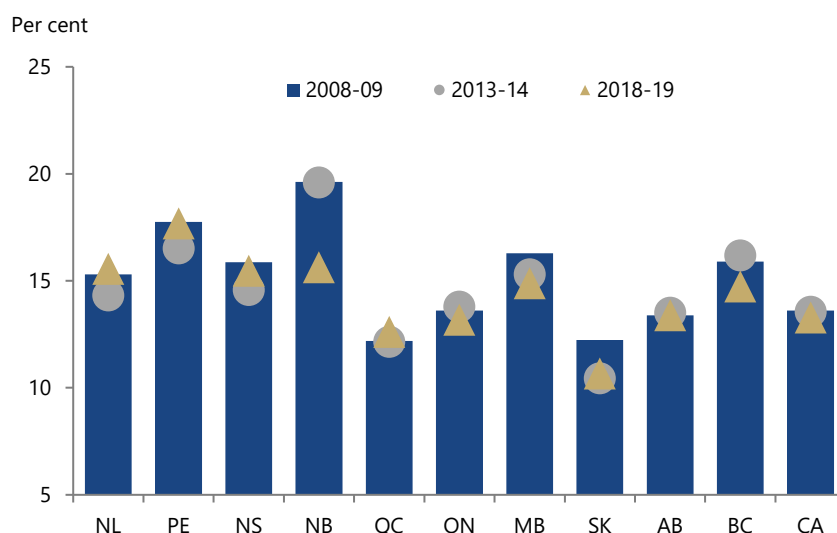
Since 2017-18, provincial and territorial governments have ramped up spending in education and social services, with growth reaching 5.7 per cent in 2017-18 and 5.4 per cent in 2018—close to double the rate of the CST over the same period, and significantly higher than growth in their spending in the previous five years.

In 2018-19, federal CST support for provincial spending in CST-targeted categories ranged from 10.7 per cent in Saskatchewan to 17.7 per cent in Prince Edward Island (Figure 4-7). Given the equal per capita allocation of CST payments, this variation is due to differences in per capita social spending across provinces, which reflect provincial government spending decisions and demographics (Figure 4-8).

Over the 2008-09 to 2018-19 period, most provinces and the Territories (combined) observed a decrease in federal CST support relative to their CST-targeted spending.

Figure 4-7

## CST as a proportion of spending on CST-targeted social spending

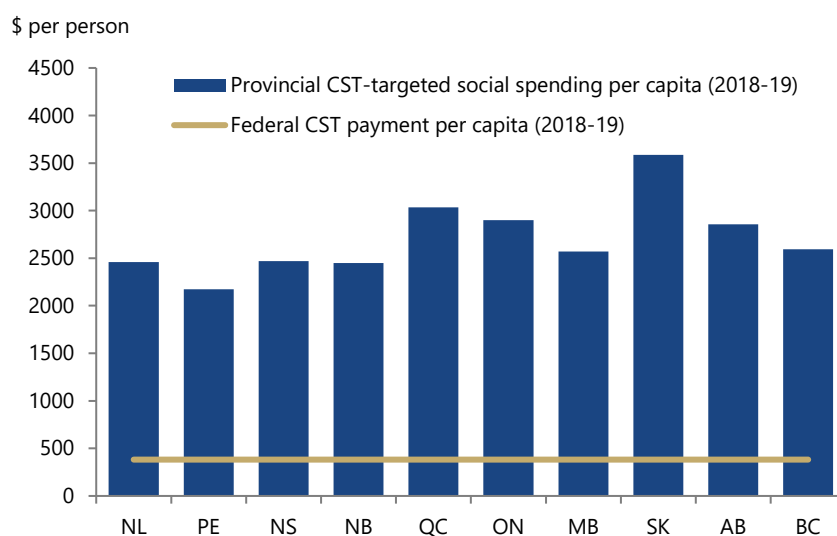


Sources: Finance Canada, Statistics Canada and Parliamentary Budget Officer.

Note: For the Territories (combined), CST support was 5.1 per cent in 2008-09, 5.2 per cent in 2013-14 and 5.3 per cent in 2018-19.

Figure 4-8

## Per capita targeted provincial social spending and CST



Sources: Statistics Canada, Finance Canada and Parliamentary Budget Officer.

Note: For the Territories (combined), per capita targeted social spending amounted to \$7,218 in 2018-19.



The largest decrease in federal support occurred in New Brunswick (4.0 percentage points), with its CST payments growing at an average of 2.2 per cent per year, while targeted spending grew at 4.6 per cent annually, on average, over 2009-10 to 2018-19—the highest growth in social spending in Canada.

Quebec and Newfoundland and Labrador were the only provinces to observe an increase in federal CST support relative to their social spending over the period 2008-09 to 2018-19. This increase in support reflects their below-average growth in targeted social spending. Quebec and Newfoundland and Labrador registered the lowest growth in CST-targeted spending among provinces. The Territories (combined) also saw their federal CST support increase over this period, from 5.1 per cent in 2008-09 to 5.3 per cent in 2018-19.

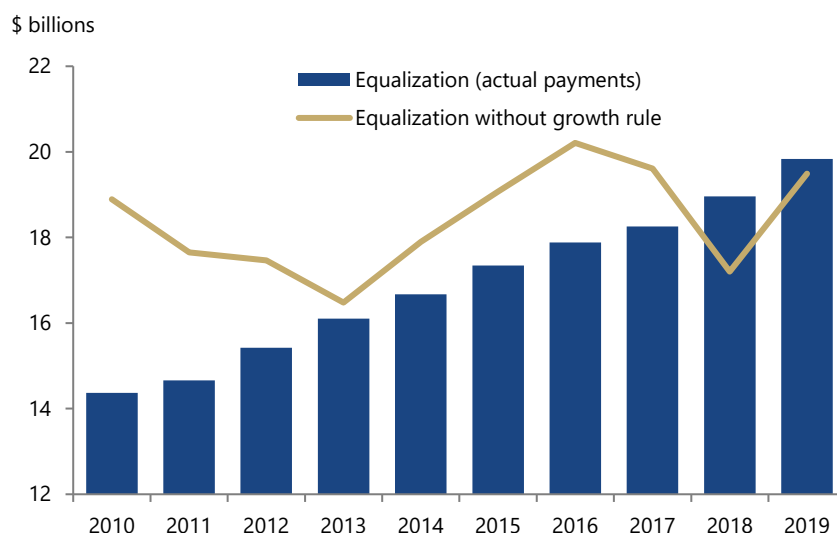
### 4.3. Equalization

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Since 2010-11, the rule constraining growth in Equalization has tended to under-equalize fiscal capacities, resulting in a cumulative savings of \$14.5 billion by 2019-20. However, beginning in 2018-19, the growth rule resulted in over-equalized payments. That is, actual Equalization payments made to provincial governments exceeded the amount necessary to (exactly) increase their fiscal capacity up to the national standard.

Figure 4-9 compares total Equalization payments under the existing program structure to hypothetical payments that would have been made had the growth rule not existed. These estimates are based on Finance Canada data.<sup>15</sup> Over 2010-11 to 2017-18, as a result of the growth rule, actual Equalization payments fell short of the payments required to bring recipient provinces up to the national standard, that is, to equalize their fiscal capacities.

**Figure 4-9** Equalization payments, with and without the growth rule



Sources: Finance Canada and Parliamentary Budget Officer.

Note: Data are in fiscal years (2010 corresponds to fiscal year 2010-11).

This situation was reversed in 2018-19 and 2019-20 when (again, due to the growth rule) actual Equalization payments exceeded the amounts necessary to bring recipient provinces' fiscal capacities up to the national standard. This dynamic broadly corresponds with the decline in economic disparities observed over the same period, especially given that the growth rule is based on a 3-year moving average (Figure 4-10).

The disparity index shown below is constructed as the standard deviation of nominal GDP per capita across provinces in a given year, divided by the average level of nominal GDP per capita (that is, the coefficient of variation).<sup>16</sup>

**Figure 4-10****Index of disparities in nominal GDP per capita across provinces**

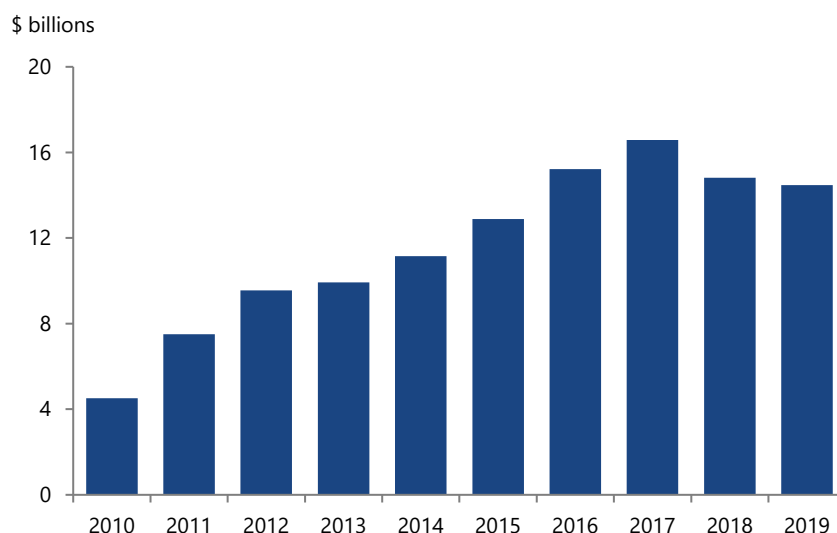
Sources: Statistics Canada and Parliamentary Budget Officer.

Note: The nominal GDP per capita disparity index is based on the coefficient of variation of nominal GDP per capita among provinces.

The growth rule appears to have prevented a significant increase in Equalization payments that would have otherwise occurred after the 2009 recession (Figure 4-11). Indeed, by 2017-18, cumulative federal savings resulting from the growth rule amounted to \$16.6 billion. Recent payments, however, have over-equalized receiving provinces by \$2.1 billion, resulting in cumulative savings of \$14.5 billion in 2019-20.

Figure 4-11

## Cumulative federal savings in Equalization payments from growth rule



Sources: Finance Canada and Parliamentary Budget Officer.

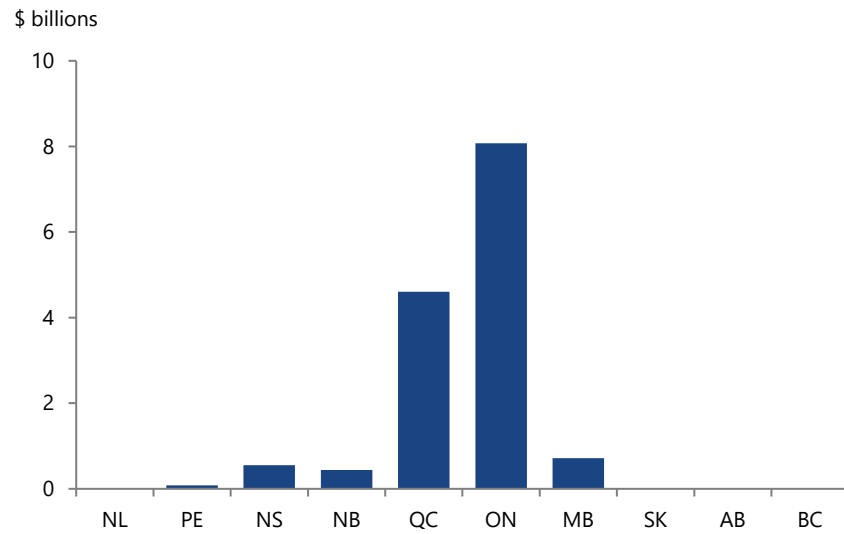
Note: Federal savings in Equalization payments is calculated as the actual payment less the payment that would be made without applying the growth rule. Data are in fiscal years (2010 corresponds to fiscal year 2010-11).

Since the growth rule was implemented in 2010, six provinces have been ongoing recipients of Equalization payments. Newfoundland and Labrador, Saskatchewan, Alberta and British Columbia did not receive Equalization payments during this period. As well, beginning in 2019-20, Ontario was no longer a recipient.

On a cumulative basis, Ontario accounted for \$8.1 billion of the \$14.5 billion in federal savings resulting from the application of the growth rule to Equalization payments (Figure 4-12). Quebec was the next largest contributor, accounting for \$4.6 billion.

**Figure 4-12**

**Cumulative federal savings in Equalization payments from the growth rule, 2010-11 to 2019-20**



Sources: Finance Canada and Parliamentary Budget Officer.

Note: Federal savings in Equalization payments is calculated as the actual payment less the payment that would be made without applying the growth rule.

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# Notes

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1. Territorial governments also receive federal transfers through Territorial Formula Financing (TFF). This is an unconditional transfer to enable territorial governments to provide “a range of public services comparable to those offered by provincial governments, at comparable levels of taxation”. For additional detail, please consult: <https://www.canada.ca/en/department-finance/programs/federal-transfers/territorial-formula-financing.html>. Analysis of TFF is beyond the scope of this report.
2. For example, see PBO’s 2018 report, *Federal Financial Support to Provinces and Territories: A Long-term Scenario Analysis* (available at: [https://www.pbo-dpb.gc.ca/web/default/files/Documents/Reports/2018/Fed%20Transfers/Fed%20Transfers\\_Prov\\_Territories\\_EN.pdf](https://www.pbo-dpb.gc.ca/web/default/files/Documents/Reports/2018/Fed%20Transfers/Fed%20Transfers_Prov_Territories_EN.pdf)); IFSD, (2017) *CHT and the Federation: Past, Present, and Future* (available at: <http://www.ifsd.ca/web/default/files/Presentations/Reports/CHT%20and%20the%20Federation%2017009.pdf>); and Fraser Institute, (2016) *Are the Provinces Really Shortchanged by Federal Transfers?* (available at: <https://www.fraserinstitute.org/sites/default/files/are-the-provinces-really-shortchanged-by-federal-transfers-rev.pdf>).
3. Although the CHA makes no explicit reference to the territories, the *Federal-Provincial Fiscal Arrangements Act* indicates that territories are included in the calculation of the CHT, and that the CHT is subject to the conditions in the CHA.
4. Available at: [http://www.scics.ca/wp-content/uploads/CMFiles/800042005\\_e1JXB-342011-6611.pdf](http://www.scics.ca/wp-content/uploads/CMFiles/800042005_e1JXB-342011-6611.pdf).
5. The CHT series used in this report includes transitional payments to provinces and territories. These payments were made to ensure no province or territory would receive less than they would have under the previous combination of cash and tax points.
6. Social assistance was defined as “aid in any form to or in respect of a person in need”. See Section 24.9.
7. Two sets of calculations are produced: 1) Equalization entitlements when provincial fiscal capacities exclude natural resource revenues; and 2) Equalization entitlements when provincial fiscal capacities include 50 per cent of natural resource revenues. A province’s initial Equalization entitlement corresponds to the larger of the two amounts calculated.
8. As stated in Budget 2009, “...Equalization has grown by 56 per cent since 2003-04. This rate of growth is clearly not sustainable.” (Department of Finance, 2009)
9. Data from CIHI include provincial, territorial and municipal governments, as well as social security funds.



10. Estimates from CIHI suggest home and community care represented roughly 0.04 per cent of provincial and territorial health care spending from 2013 to 2018 (CIHI, 2019).
11. To calculate the CST-targeted municipal and social security spending for each province and the Territories, we estimated the CST components as a share of municipal and social security spending at the national level and multiplied it by the level of municipal and social security spending in each province/territory.
12. The \$119.3 billion of CHT-targeted provincial-territorial spending in 2018-19 represents 69.4 per cent of total provincial-territorial government health spending as measured by CIHI. This share has decreased from 70.4 per cent in 2008-09.
13. Federal support through the CHT in Newfoundland and Labrador decreased from 24.66 to 24.61 per cent of targeted provincial health spending over 2008-09 to 2018-19.
14. The \$105.5 billion of CST-targeted provincial-territorial spending in 2018-19 represents 62.3 per cent of total provincial-territorial government social services spending as measured by Statistics Canada's CCOFOG. This share was unchanged 2008-09.
15. Specifically, these amounts represent Equalization entitlements after the fiscal capacity cap has been applied but before the growth rule is implemented.
16. The average used in our index is based on the national average that is, a weighted average of provincial GDP per capita levels.