Intelligence MEMOS

From: Don Drummond

To: Prime Minister Justin Trudeau and Minister of Finance Chrystia Freeland

Date: May 13, 2021

Re: **Promised Increase in the Canada Health Transfer**

The day after the April 19 Budget, the Prime Minister promised a post-pandemic increase in the Canada Health Transfer (CHT). No amount was specified, but the premiers want an immediate $27.6-billion increase to the $43 billion allotted this year, followed by larger amounts annually.

They argue future healthcare costs will increase 5 percent per annum and the burden will fall disproportionately on provinces as the current CHT formula is linked to growth in nominal GDP. This is unlikely to hit 5 percent, which will insulate federal finances to a degree.

The claim of federal fiscal flexibility can be challenged, not least by the constraint of big spending outlined in the Budget. In addition, provincial costs may not rise as rapidly as premiers project. Provincial budgets have showed lower post-pandemic healthcare spending growth rates recently. As well, there are lessons to be learned from the 2006-2016 period when 6-percent CHT growth did not bring sector improvements.

The 2021 Budget depicts precarious federal finances. It sees no return to pre-pandemic debt levels until 34 years from now, and only under optimistic assumptions for growth and interest rates. Slight but credible tweaking to those assumptions produces the result of an ever-rising federal debt burden, back to the territory of the mid-1990s fiscal crisis. And that is without any further spending increases, such as to the CHT.

The risks associated with the debt burden already make a strong case for federal tax increases. An increase in the CHT would need to be matched to a revenue source. Hiking the GST would be the preferred approach to minimize economic damage. Federal tax increases should in turn raise questions of the accountability and efficiency of one level of government raising funds another level will spend.

As provinces grappled with their fiscal challenges, they kept annual health spending growth to 3.6-percent from a 2010 base until the pandemic hit. Post-pandemic, such restraint may resurface. Ontario, as an example, projects in its budget that healthcare spending will increase 2.6 percent from 2019-20 to 2029-30. In Newfoundland and Labrador this week, meanwhile, the Economic Recovery Team recommended a 4.15-percent annual reduction in grants to health authorities for six years.

If such restraint emerges post-pandemic, the existing CHT formula will not necessarily further lower the federal share of health costs.

The 2004 Health Accord between the federal and provincial governments was to improve access, effectiveness and efficiency of the healthcare sector. But 10 years of 6-percent annual CHT growth produced little more than higher compensation in the sector. How would higher funding be used in future; to acquiesce to spending pressures or to achieve reform?

Canada faces serious economic and fiscal challenges. High debt burdens federally and provincially put the country at risk. Healthcare spending growth may elevate those risks. Debate over how the tab is split will not resolve the challenges.

A national response is required on several fronts. Economic growth must be raised to provide the needed funding for programs. Healthcare must be reformed to make more and better use of technology; improve health records; shift from an almost unique focus on health restoration to health promotion; re-orient toward home care and community-based alternatives over traditional long-term care, control if not lower drug costs and make fuller use of scope of practice for each sort of health professional.

All components of spending must be restrained to accommodate the resource shift necessitated by an aging population. CHT change is but one step in the journey.

One viable option for that step, given the risk inherent in the current specification of the CHT with unknown trends and swings in GDP, is to give the provinces and territories more certainty in funding, coupled with a modest increase in the CHT's escalator, say from the current minimum of 3 percent to something in the 4 to 4.5-percent range. That would maintain the financial imperative for all governments to take on the needed reform to healthcare.

And that would force all governments to address the need to increase taxes if they plan to keep spending growing strongly. This could even be done co-operatively if the provinces formally requested the federal government to increase the GST with the proceeds transferred to provinces. A new CHT regime could be made effective mid-decade so the provinces are not denied the lift to CHT under the current formula that will come from strong nominal GDP growth.

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