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Constitutional Reform by Stealth!

In recent years, it has become part of the Canadian identity to say that our social programs are an essential part of the Canadian identity. Oddly enough, this claim is made both by those who fight to preserve our embattled social programs and by governments which have been transforming (mainly cutting) them over the past decade. Paradox is apparently another defining Canadian characteristic.

Canada's "bifurcated welfare state" reflects and helps constitute its confederal system of government.[2] The federal government delivers major social programs, including old age pensions (Old Age Security, the Guaranteed Income Supplement and the Spouse's Allowance), the Canada Pension Plan, Unemployment Insurance, the Child Tax Benefit and veterans' benefits. The provinces also operate important social programs, including medicare, welfare, social services and Workers' Compensation. Both levels of government payout billions of dollars in benefits each year in the form of income tax breaks (credits, deductions and tax preferences), and both are involved in training and other employment services.

But the federal government also shares part of the cost of most social programs – welfare, social services, health and postsecondary education – that fall within provincial jurisdiction. During the 1950s and 1960s, when Canada's economy burbled along at a heady 5.6 percent average real rate of growth each year and governments generally collected more than they spent, Ottawa bought its way into the pro-vincial social policy field. Partly by transferring some of its taxing power to the provinces and partly by paying them cash transfers, the federal government footed a sizable portion of the provinces' growing health and welfare bills.

Federal funds enabled the provinces to build and develop social security systems far beyond what they could have afforded on their own, particularly the 'have-not' provinces. Virtually all Canadians have benefited at some point in their lives from one or another of the federally-assisted provincial social programs – from health care to postsecondary education to social assistance (welfare) to social services.

Most people have a pretty good idea of what medicare, postsecondary education and welfare mean, but social services is a fuzzy concept for many. 'Social services' is a catch-all term covering a wide range of supports to Canadians with varying needs and problems,

including child care for children in low-income families; visiting homemakers, home supports and personal supports for seniors and persons with disabilities (e.g., technical aids and equipment, attendant services and respite services for parents caring for children with severe disabilities); counselling, casework, assessment and referral services (including child welfare services for neglected and abused children in need of protection); rehabilitation services (e.g., life skills training, job referral and placement) for chronically unemployed people; community development services aimed at helping members of disadvantaged communities improve their social and economic conditions; non-insured hea1th benefits (e.g., prescription drugs, dental and eye care); and legal aid.[3] Social services are often preventive in intent and effect, helping people deal with their difficulties before they grow into more serious problems that require more costly treatment.

Naturally, the federal money came with strings attached, but fewer than many people believe. Federal payments under the Canada Assistance Plan (CAP) for welfare impose only one must-not (no residence requirements) and three musts (welfare must be available to all persons in need, there must be an appeals process and the provinces must provide certain basic program information to Ottawa).[4] The only condition under CAP for federal support of social services is that the latter must be limited to persons in need or likely to become in need if the service is not provided. Federal transfers under Established Programs Financing (EPF) for insured health care require that the provinces adhere to the five condi-tions of medicare set out in the Canada Health Act (comprehensiveness, universality, accessibility, portability and public administration). There are no conditions attached to federal transfers under EPF for postsecondary education.

The adolescent growth spurt of Canadian social policy during the 1960s has been dubbed the era of 'cooperative federalism,' but at the end of the day it was cold federal cash that secured and maintained the provinces' cooperation. The federal government made the provinces an offer they couldn't refuse – money to help fmance the social programs and health care system desired by a growing population with visions of a just society dancing in their heads. Ottawa paid half the tab for welfare and social services only if the provinces met the conditions imposed by the Canada Assistance Plan. Provinces that allowed violations of the Canada Health Act – e.g., allowing doctors to 'extra-bill,' a direct charge on patients that went against the accessibility condition – risked a cut in their federal transfer payments under EPF.

While fiscal federalism was a vital force for building and developing Canada's social security system, it began to look too rich for Ottawa's blood as the era of surpluses or small deficits that financed the expansion of the welfare state gave way in the late 1970s and 1980s to deepening deficits, mounting national debt and escalating debt financing costs. The Mulroney government put federal transfers to the provinces on a diet by partially de-indexing and then freezing EPF and by placing a ceiling on federal CAP payments for welfare and social services in Ontario, Alberta and British Columbia (the 'cap on CAP').

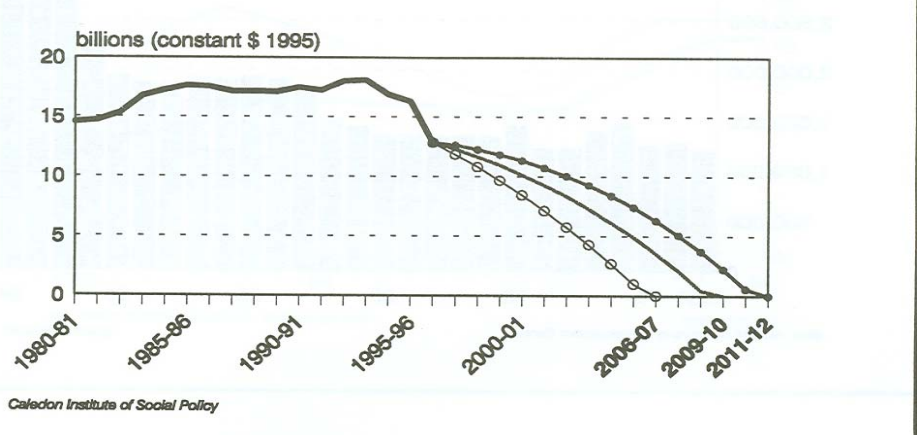
The 1995 federal Budget announced a new Canada Health and Social Transfer (CHST) that will replace the Canada Assistance Plan and Established Programs Financing in 1996-97 with a single block fund for health care and human services. The new legislation will arrive with a big cut – $2.5 billion in 1996-97, $4.5 billion in 1997-98 – in return for which the provinces will have pretty much a free hand to design and

operate their health and welfare systems as they wish. The only strings left will be the prohibition of residency requirements for welfare and the five conditions of medicare as spelled out in the Canada Health Act. The federal Minister of Human Resources Development was handed the challenging task of seeking his provincial and territorial colleagues' cooperation in "developing, though mutual consent, a set of shared principles and objectives that could underlie the new transfer.. [so that] all governments could reaffirm their commitment to the social well-being of all Canadians." [6]

Caledon has proposed a set of objectives, principles, conditions, standards and 'best practices' for the new Canada Health and Social Transfer.' However, we recognize that our best efforts in this regard – and those of the Human Resources Development Minister – probably will turn out to be Quixotic. While Ottawa and the provinces may manage to craft a list of vague objectives and motherhood principles, the engine of fiscal federalism – enforceable conditions and meaningful standards – will rapidly lose power over time and eventually will sputter to a halt. The CHST's fatal flaw is its declining cash transfer to the provinces.

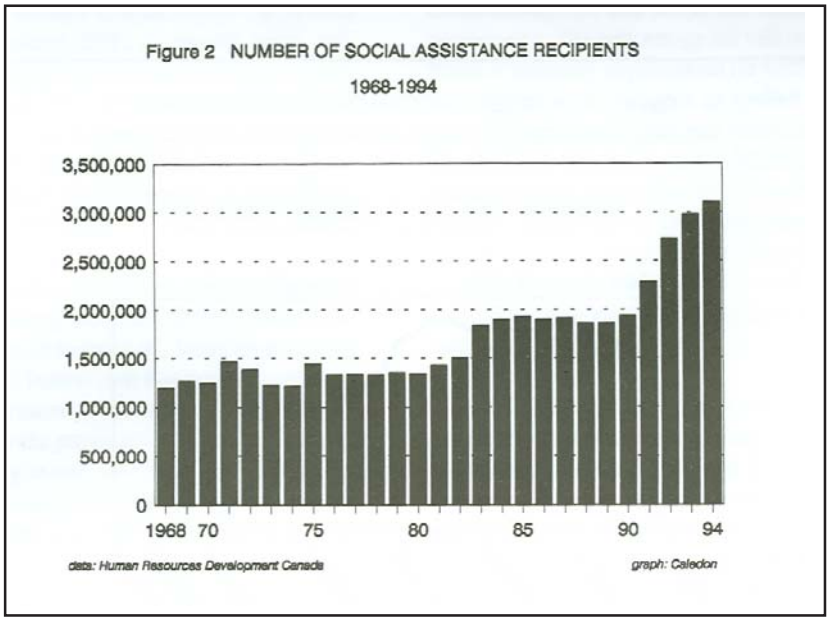
All the provinces and territories will suffer a significant reduction in their federal cash transfers when the Canada Health and Social Transfer is put in place. Under the old system (CAP and EPF), federal cash transfers to the provinces amounted to $17.2 billion in 1994-95; in 1996-97, the first year of the CHST, the provinces will get $12.6 billion (in inflation-adjusted 1995 dollars) – a substantial 26.8 per-cent real reduction. The losses will vary from one province and territory to another, ranging from 19.1 percent in Alberta to 38.4 percent in Quebec, but will be sizable everywhere. But this is only the tip of a rapidly-melting iceberg.

Figure 1 TOTAL FEDERAL CASH TRANSFERS TO PROVINCES FOR WELFARE, SOCIAL SERVICES, HEALTH AND POST-SECONDARY EDUCATION



The Canada Health and Social Transfer, like its predecessor EPF, will maintain the fIction that the federal government pays part of its transfer to the provinces in the form of tax points and the remainder in cash. Ottawa ceded part of its taxing powers to the provinces in the 1960s and 1970s in order to strengthen their revenue-raising muscle for financing their social programs; by the time that EPF was legislated (1977), Ottawa had given the provinces in total 13.5 percentage points of personal income tax and 1 percentage point of corporate tax. Only in the (not unrelated) worlds of Alice in Wonderland and Canadian fiscal federalism would the federal government try to pretend that provincial revenue-raising capacity is equivalent to a federal transfer payment. It is hard to imagine Ottawa taking back taxing powers it gave to the provinces two decades ago, let alone exercising control over this provincial revenue source.

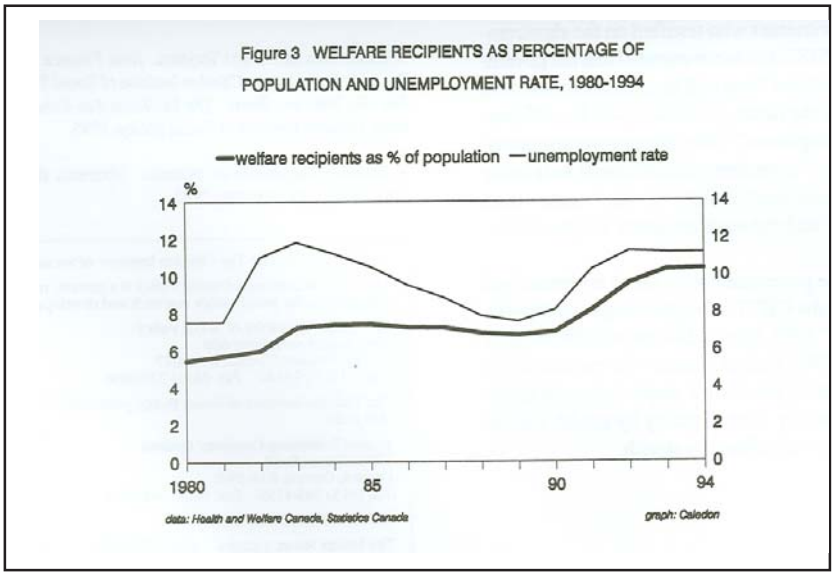
Pretend tax points or no, the CHST will have a very real and potentially devastating impact on provincial health and welfare systems.[8] Because the CHST almost certainly will be partially indexed (like EPF), or (worse still) unindexed, the real federal transfer – the cash – will decline steadily year by year and will disappear altogether in 10 to 15 years. As the federal cash dries up, so also will federal influence over provincial health and social welfare programs. As the federal cash dries up, the provinces will be left to carry an increasing burden and fmally the full weight of their costly health care and social expenditures. The almost certain result will be increasing competition for shrinking federal funds among provincial welfare, health and postsecondary education ministries; cuts in welfare benefits and, in some provinces, trainfare, volunteerfare or work-for-welfare; rising tuition fees; and growing pressures to allow the reemergence of user fees in the health care system and to shrink the range of insured services.



The year that the federal cash runs out de-pends on several factors, notably the design of the CHST and each province's performance in raising revenues in future. Caledon has projected three sce-narios, illustrated in Figure 1. In Scenario 1, the CHST is partially indexed (to the increase in GDP minus three percentage points) and adjusts for changes in provincial population, as did EPF; the cash will run out in 2011-12. In Scenario 2, the CHST is partially indexed but does not factor in provincial popu-lation changes, in which case the money disappears in 2009-10. Under the worst-case Scenario 3, the CHST is not indexed and does not take into account provincial population trends; the cash stops in 2006-7. The date the federal money ends will vary to some extent from one province to another, depending on their revenue-raising performance, their population growth and their particular mix of tax and cash transfers when the CHST comes into effect in 1996-97. Quebec could see its federal cash vanish as early as 2002-03.

The bottom line, however, is not *when* the federal cash disappears but the fact that it *will* bottom out. Moreover, the CHST will cease to exist as a political force years before it technically runs dry, since the amount of the federal cash transfer will dwindle rapidly. Without the carrot and stick of federal funds, all the talk of objectives, principles and national standards in health and social welfare is just that – talk. In the world of fiscal federalism, as in business, it's money that talks.

The federal government must maintain the fiscal in fiscal federalism. The only way to do this is to abandon the Mad Hatter fiction of tax points and treat the Canada Health and Social Transfer as a cash payment only, fully indexed to the performance of the economy as measured by the change in GNP. Obviously, the federal government still would want to reduce its current level of cash transfer payments, perhaps even more than it announced in the 1995 Budget (since it would be foregoing its enormous future savings



from the decline of the CHST cash transfer). However, there is a world of difference between an ever-declining-to-eventually-disappear CHST and a CHST that substantially reduces – but then sustains – a stable and predictable federal fiscal (and political) presence in provincial social programs.

One of the strengths of the Canada Assistance Plan (until the 1990 cap on the three 'have' provinces) is that it guaranteed federal fmancial support to the provinces when they most needed it – during recessions, when rising unemployment throws many unemployed Canadians onto the welfare safety net because they exhaust their ill benefits or do not qualify for ill. If the federal government withdraws its funding of provincial welfare, then the provinces will be hit hard when the next recession arrives. We need only look at Ontario's experience during the most recent recession to see the shape of things to come; squeezed between rising welfare caseloads and the cap on CAP, Ontario lost $7.7 billion in federal support between 1990-91 and 1994-95 and saw Ottawa's share of the province's welfare and social service expenditures fall from 50 to 29 percent in just a few years.

Figure 2 shows the trend in the number of women, children and men on welfare from the inception of the Canada Assistance Plan in the late 1960s until 1994, the latest year for which figures are available. The number of welfare recipients rose noticeably in the early 1980s as a result of the 1980-81 recession, from 1.4 million in 1980 to 1.9 million in 1984; levelled off during the mid-1980s; then rose sharply again with the latest economic downturn, reaching a record 3.1 million in 1993.

Figure 3 shows that the trend in the percent-age of welfare recipients has moved in the same di-rection as the unemployment rate in the 1980s and 1990s. In 1980, welfare recipients comprised 5.4 percent of the population, but rose to more than 7 percent after the 1980-81 recession and then jumped with the most recent recession to a peak of 10.4 percent in 1994. While the substantial increase over the years in the welfare case load is also the result of other factors such as rising marriage breakdown, the restructuring of the labour market, de-institutionalization of persons with disabilities and cutbacks to Unemployment Insurance, higher unemployment clearly puts added pressure on the welfare system – and the governments (make that government, once the federal money runs out) that fund it.

Not only should Ottawa deliver the CHST as a fully-indexed cash payment, but it also should ensure counter-cyclical protection for a portion of the transfer for welfare. This could be accomplished by designating a certain portion of the CHST for welfare and building into the annual indexation formula an indicator of demand, such as the percentage of each province's non-elderly population that is not employed.

Although the Liberal government is an avowed opponent of the 'social policy by stealth' practised by its Conservative predecessor, the CHST will be a stealthy program if it is not fully indexed and designed as a cash payment. It is heartening that the Commons Standing Committee on Finance, which listened to witnesses who testified on the shortcomings of the CHST, has recommended that the government "commit that there will be a cash component to the CHST in the future, and that it will be sufficient to enforce compliance.''[9] The federal govemment can-not profess its "commitment to the social well-being of all Canadians" while at the same time pulling the fiscal rug out from under the provinces.

If the government goes ahead as planned and fails to stem the CHST's disappearing cash

transfer, the Liberals' 1995 federal Budget will finish what the Tories' 1986 Budget started – the erosion of the federal spending power in a major sphere of Canadian public policy. Social policy by stealth will effect constitutional reform by stealth.

Ken Battle

Notes

1. Ken Battle (under the pseudonym Grattan Gray) coined the tenn and introduced the concept of policy by stealth in his cri-tique of Conservative social and tax policies, "Social Policy by Stealth", *Policy Options,* March 1990. The phrase has become part of the discourse of Canadian public policy, having been used by academics, editorial writers, social advocates, professional associations and politicians including the current federal Ministers of Finance and Human Resources Development.

2. Banting, Keith. (1987). *The Welfare State and Canadian Federalism.* Second edition. Kingston and Montreal: McGill-Queen's University Press, p.58.

3. Human Resources Development Canada. (1994). *Reforming the Canada Assistance Plan: A Supplementary Paper.* Ottawa: Minister of Supply and Services Canada, pp. 5-6.

4. Torjman, Sherri and Ken Battle. (1995). *Can We Have National Standards?* Ottawa: Caledon Institute of Social Policy, May.

5. Mendelson, Michael. (1993). *Social Policy* in *Real Time*. Ottawa: Caledon Institute of Social Policy, pp. 4-5.

6. Canada. (1995). *Budget Plan.* Tabled in the House of Commons by the Honourable Paul Martin Ottawa: Department of Finance Canada, p. 53.

7. Torjman, Sherri and Ken Battle. (1995). *Can We Have National Standards* ? Ottawa: Caledon Institute of Social Policy, May.

8. Battle, Ken and Sherri Torjrnan. (1995). *How Finance Re-Formed Social Policy.* Ottawa: Caledon Institute of Social Policy. See also Torjman, Sherri. (1995). *The Let-Them-Eat-Cake Law.* Ottawa: Caledon Institute of Social Policy.

9. Standing Committee on Finance. Sixteenth Report. Ottawa: House of Commons, 1995. Copyright@ 1995 by The Caledon Institute of Social Policy.

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