

Slicing the Pie

Principles for Allocating Transfer Payments
in the Canadian Federation

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Executive Summary

Only about one-third of the funds that Canadians send to the federal government go directly towards federal operations and programs. The other two-thirds are redistributed through transfers to provinces and territories, people, and organizations. The effect of these transfers on regional redistribution, with revenues collected in some areas of the country and spent in other areas, is significant. In fact, the combined redistribution through these transfers is greater than the formal redistribution undertaken through the Equalization program.

While the Equalization program is often a focus of heated debate, the approaches used to determine each province's allocation of other transfers are often undertaken on an unprincipled basis. The published formulae often lack transparency or are sometimes unavailable entirely. The uneven distribution of billions of dollars of federal spending too often comes without a clear, public explanation for why some provinces get more and others get less.

Unprincipled allocation of federal fiscal transfers is corrosive to the federation. It contributes to mistrust between governments and citizens and makes collaborative intergovernmental action more difficult. A lack of transparency in allocations makes it all the easier for residents of all provinces to believe that somehow they are getting shortchanged. This contributes to heightened inter-regional tension.

It does not have to be this way. In fact, the federal government made a commitment to moving towards principled allocations of federal fiscal transfers in their 2007 budget.¹ As a result of that commitment, the federal government moved toward principled allocations in the Canada Social Transfer and the Canada Health Transfer. But the progress made then stalled—and in some cases has been reversed.

In our assessment of the way federal transfers are allocated, we find a mixed picture. A number of transfers do have clearly stated and reasonably fair principles for allocation. For others, there are major deviations from a principled approach and no public explanation offered as to why. Addressing these distortions is important for both a coherent approach to fiscal federalism and a more transparent accounting to Canadians. Significant, unexplained deviations from principled allocation approaches can also be a source of public cynicism and intergovernmental or inter-regional tensions.

Unprincipled allocation is felt by people in real ways. It is felt by workers in Ontario who have access to fewer funds for job training. It is felt by people with disabilities in Quebec, where the province receives less than an equal per capita share of Labour Market Agreement for Persons with Disabilities funding to provide employment supports to those who need it. It is felt by people in British Columbia who have less access to social housing.

¹ Finance Canada. 2007. *Budget 2007*. <http://www.budget.gc.ca/2007/pdf/bp2007e.pdf>

The path forward is both clear and achievable. We propose four guiding principles to determine the appropriate approach for allocating federal transfer payments throughout the federation. Allocations should be:

- » Clear and transparent
- » Fair to Canadians regardless of where they live
- » Consistent with the policy objectives of the transfer
- » Predictable, with the flexibility to adapt to changing circumstances.

Unprincipled allocation is felt by people in real ways.

Allocations consistent with these principles could take a variety of forms. Comparative experience in federations highlights four different kinds of principle-based allocations that can be used, depending on circumstances:

- » Per capita
- » Per client
- » Need-based
- » Merit-based

Our review of comparative experience found that other federations overwhelmingly use these approaches.² In Canada we also use all of them, but not consistently and with too many exceptions. We also found that in other federations governments regularly reported on which approach they used and why—because using the wrong principle-based approach in the wrong situation (for example, adopting a per capita approach when a per client approach should be used) undermines transparency and policy goals.

Because the federal government does not consistently use principle-based approaches, Canadians in different parts of the country have different access to essential public services funded with their federal tax dollars. In particular, funds for training, infrastructure and housing defy logic and deprive some Canadians—in all these cases, Ontarians—of equitable access to programs and services.

There is no reason why the federal government should not move immediately to a principle-based approach for all fiscal transfers. There is also no reason that it should not report publicly on its allocation decisions and their rationale. Since the federal commitment in 2007 to move to a principle-based approach, it has failed to do so. There is no explanation for this that we can see.

2 see: Hjartarson, Pearce, and Mendelsohn, Nov 2010. *A Report Card on Canada's Fiscal Arrangements*. http://mowatcentre.ca/wp-content/uploads/publications/12_a_report_card_on_canada.pdf; Boadway and Shah, 2007. *Intergovernmental Fiscal Transfers: Principles and Practice*. World Bank.

Introduction

The federal government is in part a financial clearing house, raising revenue on a national basis and distributing it throughout the country. Every year, roughly two-thirds of the \$246B federal program budget is distributed to provinces and territories, organizations, and people through transfer payments of all types.³ How these are allocated has an enormous impact on Canadians and provincial governments.

Discussion of fiscal federalism in Canada typically focuses on the Canada Health Transfer, Canada Social Transfer, Equalization and Territorial Formula Financing. Together, these high profile payments account for the bulk of transfers to other levels of government in Canada.⁴ But these large block transfers are only part of the picture.

The \$163B includes other transfers to provinces to deliver core economic and social programs like infrastructure development and housing, as well as transfers to people (like Old Age Security and Employment Insurance) and support to businesses and non-profit organizations. All of these matter if you want to understand the net impact of the transfer payment system.

³ Public Accounts of Canada data for 2012-13, based on spending before debt service

⁴ Calculations of program spending exclude debt servicing charges.

1 First Principles

Just as Canadians expect government program spending to be accounted for in a clear and transparent manner, the same principle should apply to the way these transfers are allocated. If Canadians cannot clearly see where their tax dollars are going and why, they cannot properly hold their governments to account. Deviations from well-established principles should be rare exceptions, explained transparently and subject to open debate.

While every federation is unique, there are some useful lessons that Canada can take from the way other countries operate. In their 2007 World Bank study of a wide range of countries, Robin Boadway and Anwar Shah suggest maximizing simplicity and transparency, establishing clear objectives, and engaging in periodic review and renewal through an intergovernmental forum as best practices to strive for.⁵ Previous Mowat Centre reports have pointed to similar principles and examples such as Australia's streamlined and equalized transfer for social, health and education programs.⁶

Based on these best practices, we propose four main principles for the allocation of federal transfer payments. These transfers should be:

1. Clear and transparent
2. Fair to Canadians regardless of where they live
3. Consistent with the policy objectives of the transfer
4. Predictable, with the flexibility to adapt to changing circumstances

These principles provide a reasonable and consistent means for observers to judge the various approaches to federal allocation of transfers. The principles leave considerable room for flexibility. Even then, sometimes there will be good reasons for a program to be an exception to these rules. In those rare cases, we recommend simply that the rationale for this decision be communicated transparently.

Deviations from well-established principles should be rare exceptions, explained transparently and be subject to open debate.

Principle 1 Allocation approaches should be clear, transparent and understandable

For Canadians to be in a position to effectively judge how their government is spending their tax dollars, they depend on clear, understandable and accessible explanations of how allocation decisions are made. Given the significant portion of the federal budget that is redistributed throughout the country in the form of transfers, a clear accounting of regional allocation is necessary.

In a 2010 study, the Mowat Centre asked Canadian experts to rate the success of the transfer system against a set of benchmarks outlined by the World Bank.⁷ Their response was resoundingly critical. Overall, the transfer system scored a mediocre C, but the worst performing benchmark was transparency, scoring a D+.⁸ Respondents noted the tendency for allocation approaches to be unclear and easily misunderstood by both the public and governments.

⁷ Hjartarson et al, 2010 ; Boadway and Shah, 2007

⁸ Hjartarson et al., 2010. A grade of D+ was arrived at by averaging the rating given to the transparency benchmark based on the following definition: "Both the formula and the allocations should be public and disseminated widely to encourage accountability and fairness in transfers."

⁵ Boadway and Shah, 2007. pp. xxxi.

⁶ Hjartarson et. al, 2010.

In too many cases today, deciphering the actual allocation of federal transfers takes a cryptographer's eye and the patience of a monk. Even with those rare attributes, sifting through public accounts and budget data from federal and provincial governments offers no guarantee that enough information would be available to develop a coherent picture of where dollars are going. This is not a universal challenge—the Canada Health Transfer and Canada Social Transfer, for example, have clear and understandable allocation approaches—but nor is it acceptable or necessary.

Principle 2

Allocation approaches should treat Canadians fairly regardless of where they live

Canadians need to trust that the transfer system is treating them fairly and that the programs and services they rely on are not being compromised by confusing, unjustified vagaries in the allocation of funds based on where they reside. This does not mean that the federal government needs to allocate funding for port infrastructure or flood mitigation on an equal per capita basis if needs differ across the country. But nor should the approach be arbitrary—allocation approaches that define need on a basis other than population should use measures that are transparent and well-established.

This principle of fairness underpins Canadians' trust in their government. Canadians expect a government that makes decisions in the interest of all Canadians, and not narrow geographic or partisan interests. This principle reinforces that trust.

Principle 3

Allocation approaches should be consistent with the policy objectives of the transfer

The allocation approach for federal transfers should take as a guiding basis the purpose of the program. For example, the express purpose of the 2006 Off-Reserve Aboriginal Housing Trust was to “to help provinces address short-term pressures with regard to the housing needs of Aboriginal Canadians living off reserve.”⁹ The approach chosen in this case (based on the province's share of Aboriginal persons

living off reserve) is far better suited to meeting the goals of this program than an equal per capita approach would have been. Likewise, a merit-based program that created pools of funds could privilege areas with the most established service providers (which may not be the same areas facing short-term pressures). Choosing an allocation approach that is not consistent with the objectives of the transfer can be as bad as having no principle at all.

Principle 4

The approach should provide predictability for all parties, but be updated when circumstances change.

The funds distributed by transfers should be allocated according to a predictable approach, allowing provincial and territorial governments, municipal governments, third party organizations and individuals to make sound financial planning decisions. Both principles and common sense can be useful in determining how funding levels should evolve. The size of the transfer should also be in line with the policy objectives of the transfer, meaning that they do not lose real value over time, and they respond to real world changes (spikes or dips in unemployment, for example).

This does not mean however that the allocation should never change. Many of the heavily distorted allocations that exist today result from failing to re-think and update historical rationales. For example, 40 per cent of the funding for the Federal-Provincial-Territorial Labour Market Development Agreements is allocated between provinces based on the relative impact of the Employment Insurance Reforms made in 1996. For an 18 year old in the labour force today, this means funding for services they may need to draw on to adapt to today's labour market depends on circumstances from before they were born. Federal allocation approaches should incorporate feedback mechanisms and adjust to evolving circumstances.

⁹ Finance Canada, 2006. *Budget 2006*. <http://fin.gc.ca/budget06/pdf/bp2006e.pdf>

2 Putting Principles into Practice

Our proposed principles are not utopian or unreasonable. By and large, they are consistent with the best practices of federal allocation approaches today.

There is no one-size-fits-all allocation approach that meets all of these principles in all circumstances. Different policy areas and different conditions demand different responses. But a principled allocation, transparently presented and subject to public scrutiny and debate, should be the goal. Too often, dissembling is the goal, which just leads to conflict and confusion, with Canadians in all regions believing they are being treated unfairly.

Taking these principles into account, we find that there are four main approaches for federal transfers that are defensible, depending on circumstances. Each of these is used in some form today in Canada, often at the federal level. It is still possible for any of these four approaches to be unfair and unprincipled if applied inappropriately or in the wrong circumstances. However, they represent a toolkit to update the chaotic and outdated approaches that exist in too many instances today.

These four approaches are:

- » Equal per capita
- » Equal per client
- » Need-based
- » Merit-based

Equal per capita

A transfer that provides an equal amount for each Canadian is the natural starting point for a principled approach that fairly and clearly allocates federal transfers.

For federal-provincial or federal-municipal transfers, an equal-per-capita approach like the one used for the Canada Social Transfer (and as of 2014, the Canada Health Transfer) allocates to each government a share of the transfer equivalent to their share of the population. This is the starting point for a principled approach from which any deviation should have a clear and defensible rationale. Looking at fiscal federalism in practice in a comprehensive global study, Robin Boadway and Anwar Shah reinforced this point, arguing that “[i]n the absence of reasons to the contrary, transfers should be unconditional and equal per capita in allocation.”¹⁰

In general, a per capita allocation tends to do a reasonably good job of ensuring that provinces can provide comparable levels of services to their populations. While it may be true that economies of scale can be achieved in provinces with large, concentrated populations, these are generally confined to public administration, not service provision. Where this is not true, other approaches (like equal per target population or expenditure need) might be more appropriate.

While not an explicit driver of the approach, another feature of the equal per capita approach is that it has an equalizing effect—narrowing the gap between provinces’ fiscal capacity. Because federal revenues are drawn disproportionately from wealthier provinces (by virtue of their residents’ and businesses’ higher incomes) and then distributed on an equal population basis, per capita transfers have an effect of redistributing towards provinces with a weaker tax base.

¹⁰ Boadway and Shah, 2009. *Fiscal Federalism: Principles and Practice of Multiorder Governance*. pg. 332

Equal per client

A variation on the equal per capita approach is to distribute federal transfers based on a province or territory's share of the population that would be targeted for assistance by the program. This is appropriate where there is a clear and well-accepted way to identify and measure the client group's size. For transfers to persons, this means simply that each Canadian faces the same eligibility criteria and receives the same benefit according to that criteria. This is true for most federal transfers to persons, such as Old Age Security (the largest) and child benefits.

For example, the 2006 Off-Reserve Aboriginal Housing Trust was distributed on a per client basis because there was a clear set of data from the Census on each province/territory's share of Canada's population of Aboriginal people living off-reserve. This approach is well-suited for programs targeted to assist people of certain ages or other easily measured characteristics.

Some programs appear to be equal per client on the surface, but when examined more closely are skewed away from a true equal per client approach. The Settlement Funding Formula for example, is described as a way of allocating federal transfers to organizations to provide immigrant settlement services on the basis of a province's share of immigration (with additional weight for refugees).¹¹ In practice, the amount allocated per immigrant ranges significantly in a way that is not explained by proportion of refugees, and is skewed by other 'adjustments' that move the transfer away from the equal per client approach and away from a principled approach more generally.

A per capita allocation tends to do a reasonably good job of ensuring that provinces can provide comparable levels of services to their populations.

11 Citizenship and Immigration Canada. 2011. "Backgrounder—Government of Canada 2012-13 Settlement Funding Allocations" <http://www.cic.gc.ca/english/department/media/backgrounders/2011/2011-11-25.asp>

Need-based

A need-based transfer accounts for the different cost of, or demand for, providing comparable services in different parts of the country. This allocation approach can consider any number of factors that influence the cost of providing public services between regions, including demographic differences, geographic differences, and price differences.

While not commonly used at the federal level, need is used in some cases by provinces to allocate their general-purpose transfers to local governments.¹² A prototype for an expenditure need-based Equalization program was put forward by Peter Gusen in 2012 as part of Mowat's Fiscal Transfers series.¹³

An example of need-based transfers in practice can be found in Ontario education funding. The provincial Ministry of Education distributes education funding to school boards throughout the province through a set of need-based transfers, known collectively as the Grants for Student Needs. These grants take into account labour costs, capital needs, and operational costs (e.g., maintenance of facilities, school bus operation).¹⁴ They also take into account the demography and geography of each school board, including their share of high needs students.

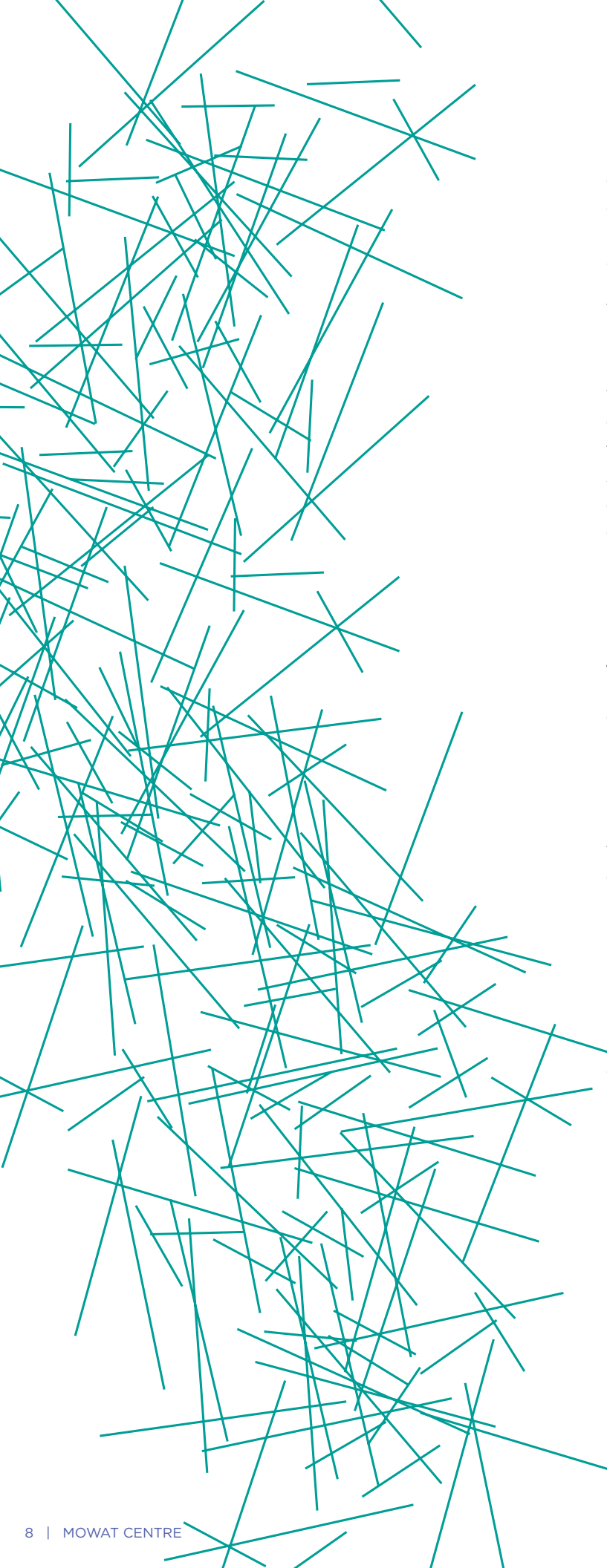
The formula is complex, but it is subject to open consultation and mandated legislated review, and the calculation and rationale are made publicly available each year. This transparency allows for constructive debate on how to improve the chosen variables and criteria each year—for example, considering the appropriate adjustment to respond to need in school boards with a high percentage of low-income households.

The advantage offered by need-based approaches is incorporating a measure of equity—ensuring that Canadians are able to access comparable services supported by their federal government at comparable levels of taxation. Some have made the case that the Canada Health Transfer should take into account expenditure need, especially demographic factors (such as a province's share of seniors, who tend to

12 Boadway and Shah, 2009. pg. 361

13 Gusen, 2012. *Expenditure Need: Equalization's Other Half*. http://mowatcentre.ca/wp-content/uploads/publications/46_expenditure_need.pdf

14 The 2013-14 formula and rationale can be found here: http://www.edu.gov.on.ca/eng/funding/1314/Technical13_14.pdf



have higher health costs).¹⁵ This equity does however come at the expense of the principle that transfers should be clear and understandable. This trade-off could be mitigated at least in part by tasking arms-length bodies with providing clear and accessible accounting of these approaches to the public.¹⁶

The greatest obstacle to incorporating need-based approaches is finding the most appropriate way to measure need. Often competing arguments can be made for need when transfers are intended for broad purposes. For example, need-based transfers in the United States tend to give more weight to rural areas to manage the costs of service delivery in low-density areas, while in Germany cities tend to get more weight to account for the costs of congestion. Need-based approaches depend on clearly accepted measurement approaches for the level of need.

Merit-based

A fourth approach to allocation that can be consistent with principles is an application-based “merit” decision. In these cases the federal government makes a pool of funding available for a program with clear criteria, and organizations (or municipalities) that meet those criteria are free to apply.

In theory, this approach can be clear and understandable, treat Canadians fairly regardless of where they live, and can be consistent with the policy objectives of a program. Naturally, an application-based program offers less predictability, but there is no reason that a merit-based program cannot provide a predictable stream of funding. The EcoEnergy Home Retrofit program, for example, provided a merit-based federal transfer to individuals with clear criteria and a predictable subsidy for their investments in home energy efficiency, so long as homeowners complied with the program’s rules.

In practice, it is important to distinguish merit-based allocation approaches that are consistent with these principles from those that are “merit-based” in name but remain opaque and complex. Merit-based programs are more appropriate when the need for a program is uneven across the country and distributional issues are secondary.

¹⁵ For example, see Di Matteo, 2012.

¹⁶ For example, see Beland and Lecours, 2012.

3 Taking Stock of Allocation Today

When we take stock of how the allocation of federal transfers takes place today in Canada we see examples of each of the major principled allocation approaches. Equal per capita is the most prevalent type of principled allocation for federal transfers. Of the \$25.7B in national federal-provincial trusts established for a variety of priorities (including health, police officer recruitment, climate change and infrastructure) between 1999 and 2008, 93 per cent were allocated on an equal per capita basis.¹⁷ As of 2014-15, the Canada Health Transfer and Canada Social Transfer are also allocated on an equal per capita basis. This represents progress.

Variations of merit-based approaches are also common (especially for economic development and infrastructure initiatives). This is a perfectly reasonable approach. But it is not always clear whether merit-based allocation formulae are in fact driving funding to the most worthwhile project or whether they are effectively being distributed on an ad hoc basis. In practice, the decision-making can be opaque and the eligibility criteria can be structured in a way to skew away from the core principles. For example, the federal Clean Energy Fund, announced in Budget 2009, earmarked a large share for Carbon Capture and Sequestration (CCS) projects in Saskatchewan, a technology of little-to-no relevance for the several provinces without coal-fired electricity generation or oil and gas extraction. While there is nothing inherently wrong with the federal government making a strategic choice to invest in research in CCS technology, it is not at all clear that this decision was based on a scientific assessment of the relative merits of CCS compared to other clean energy technologies.

Equal per client approaches, such as the Off-Reserve Aboriginal Housing Trust announced in Budget 2006¹⁸ are more rare, limited by availability of shared data and definitions. The ability to use this approach has been further weakened by cuts to Statistics Canada surveys (including the long-form census). Need-based approaches are still rarer at the federal level (though more often seen in provincial-local transfers); however an earlier Mowat Centre paper has outlined a proposed expenditure need approach to improving the Equalization program.¹⁹

Measured against the principles we present in this report, transfer allocations today in Canada present a mixed picture. The allocation approaches for most federal transfers are principled (even if they fall short on clear communication). On the positive side, a number of our major transfers to governments and to persons are largely consistent with these principles. The Canada Health Transfer and Canada Social Transfer are distributed on an equal per capita basis, while Old Age Security/Guaranteed Income Supplement and children's benefits are all distributed on an equal per client basis.²⁰ For this significant component of federal public spending, there are clear and defensible rationales, even if one could make the case that fairer approaches are available (such as taking into account differing need). On the other hand, the Equalization program, for reasons well-documented elsewhere but not explored in this report, is in need of major reforms to meet the principles laid out here.

For a smaller but substantial portion of federal transfers, the allocation approach ranges from opaque to incomprehensible to obviously unfair. As the examples in the following section show, complex formulae and historical legacies seriously distort the allocation of these transfers away from fairness, transparency, or program objectives. The federal government should take steps to bring these transfers in line with principled allocation approaches.

These distortions are not academic—they represent real funding shortfalls that shortchange Canadians in certain provinces on benefits and services, and place extra burden on some provincial governments to bridge the gap. Taxpayers in these provinces pay twice—once for the federal transfers headed elsewhere and then again to their provincial governments to pick up the slack. In the cases where the allocation approach is not clearly communicated, it is more difficult for Canadians to understand how their money is spent and to hold their governments to account. Ultimately, these unprincipled approaches undermine the shared project of the federation.

17 Mowat Centre Calculation based on Finance Canada data found here: <http://www.fin.gc.ca/fedprov/ftf-eng.asp>

18 Federal Budget 2006. pg. 114 <http://fin.gc.ca/budget06/pdf/bp2006e.pdf>

19 Gusen, 2012

20 While both transfers to governments and to individuals are framed by different economic and policy rationale, they are both important to how financial flows operate in the federation and both can adhere to the principles. This assessment is taken strictly from the lens of fiscal federalism and allocation between provinces.

4 Room for Improvement

Whether driven by decades-old circumstances, hidden rationales, or misguided equal per jurisdiction approaches, there are a long list of federal transfers that fail to meet the test of these principles. Much like how Tolstoy noted that “each unhappy family is unhappy in its own way,”²¹ each unprincipled transfer skews from a fair allocation in its own way. A brief assessment of the following four areas illustrates how the challenges of ad hoc, outdated and unprincipled allocations impact Canadians in practice.

1. Social and affordable housing
2. Infrastructure funding
3. Labour market training
4. Immigrant settlement funding

Social and Affordable Housing

Instead of being distributed on the basis of a principled allocation approach, federal funding for social and affordable housing support is divided among provinces and territories on the basis of historical legacies and generally unclear federal decisions. The result is that funding is not based on population, need, or merit.

FIGURE 1

Federal Funding for Social and Affordable Housing

PROVINCE/ TERRITORY	2011/12 FEDERAL FUNDING (\$M)	SHARE OF NATIONAL TOTAL	SHARE OF POPULATION 2011	SHARE OF CORE HOUSING NEED ²²
NL	\$56.4	2.8%	1.5%	1.8%
PEI	\$14.5	0.7%	0.4%	0.4%
NS	\$70.3	3.4%	2.8%	2.9%
NB	\$49.1	2.4%	2.2%	2.0%
QC	\$431.3	21.1%	23.3%	21.7%
ON	\$706.5	34.5%	38.6%	42.0%
MB	\$118.4	5.8%	3.6%	3.1%
SK	\$137.0	6.7%	3.1%	2.7%
AB	\$150.0	7.3%	11.0%	8.0%
BC	\$227.5	11.1%	13.1%	14.8%
NU	\$49.0	2.4%	0.1%	0.2%
NWT	\$28.7	1.4%	0.1%	0.2%
YK	\$9.5	0.5%	0.1%	0.1%

The divergence from a principled allocation approach means a significant shortfall in federal funding for the provinces that need it the most. In particular, the four most populous provinces (Ontario, Quebec, British Columbia, and Alberta), which are also home to the most expensive housing markets in Canada, all receive a good margin lower than either their share of the population or their share of the target population—those in core housing need.

21 Tolstoy, *Anna Karenina*

22 Source: For Funding Allocations: CMHC Canadian Housing Statistics 2011-12; For Core Housing Need (2006) CMHC Canadian Housing Observer Households in Core Housing Need, Canada, Provinces and Territories; Population share from Statistics Canada.

Infrastructure Funding

There are numerous federal funding programs that support infrastructure development across the country. These include the many components of the Building Canada Plan, short-term investments like the Infrastructure Stimulus Fund (ISF)—introduced in 2009 as part of Canada’s Economic Action Plan in response to the global economic downturn—as well as permanent funding streams like the Gas Tax Fund.

These programs follow a variety of allocation approaches—some of which are transparent, some of which are not. Overall, there are major divergences from a principled regional allocation. There is significant room for improvement in the approach to allocating infrastructure support, both on a global basis and within programs.

Federal infrastructure funding practices fall particularly short on the principle of remaining clear and understandable. For a number of programs, basic funding information is not readily available, and even when it is, the release comes well after the money has been spent. The shifting of funds between various programs for the 2009-11 infrastructure stimulus in particular made it very difficult to assess where money has been spent.

The divergence from a principled allocation approach means a significant shortfall in federal funding for the provinces that need it the most.

The Building Canada Fund and Base Funding Carve-outs

The federal budget of March 2013 included an announcement of further infrastructure funding through 2024 as a highlight of the budget, but was extremely thin on details. About one year later, the details of the \$14B next generation of the Building Canada Fund have been made available.²³ The welcome news is that there is a clear and understandable description of how the funding will be allocated throughout the country, bringing predictability. The unwelcome news is that the new program extends the past practice of equal per jurisdiction “base funding”, which has no relationship to population share, project merit, need or size. This is inconsistent with the principle of treating all Canadians fairly regardless of where they live and with the policy objectives of the program.²⁴

FIGURE 2
2014-2024 Funding by Province or Territory for Building Canada Plan Provincial-Territorial Infrastructure Component

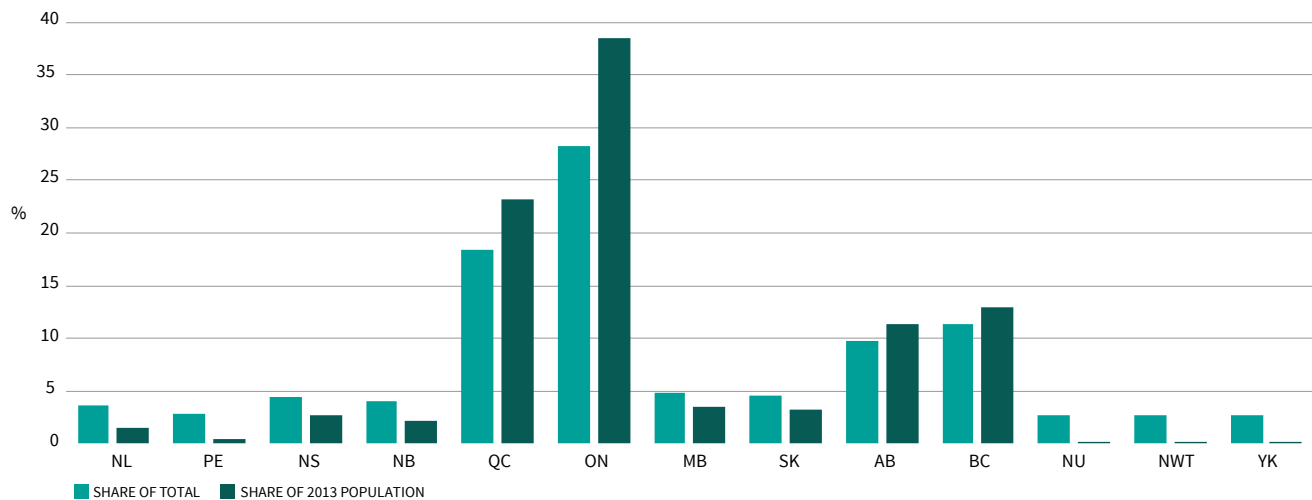
PROVINCE/ TERRITORY	BASE FUNDING	PER CAPITA PORTION	TOTAL	SHARE OF TOTAL	SHARE OF 2013 POPULATION
NL	\$250,000,000	\$99,018,276	\$349,018,276	3.6%	1.5%
PE	\$250,000,000	\$27,039,852	\$277,039,852	2.9%	0.4%
NS	\$250,000,000	\$176,494,164	\$426,494,164	4.4%	2.7%
NB	\$250,000,000	\$143,637,228	\$393,637,228	4.1%	2.2%
QC	\$250,000,000	\$1,519,473,480	\$1,769,473,480	18.4%	23.2%
ON	\$250,000,000	\$2,470,342,980	\$2,720,342,980	28.2%	38.5%
MB	\$250,000,000	\$217,085,904	\$467,085,904	4.8%	3.5%
SK	\$250,000,000	\$186,658,080	\$436,658,080	4.5%	3.2%
AB	\$250,000,000	\$691,913,376	\$941,913,376	9.8%	11.4%
BC	\$250,000,000	\$839,897,436	\$1,089,897,436	11.3%	13.0%
NU	\$250,000,000	\$6,584,172	\$256,584,172	2.7%	0.1%
NWT	\$250,000,000	\$8,054,424	\$258,054,424	2.7%	0.1%
YK	\$250,000,000	\$6,200,628	\$256,200,628	2.7%	0.1%
Total	\$3,250,000,000	\$6,392,400,000	\$9,642,400,000		

Source: Infrastructure Canada²⁴

23 Details available here: <http://www.infrastructure.gc.ca/plan/ptic-vipt-eng.html>
24 Infrastructure Canada. <http://www.infrastructure.gc.ca/plan/ptic-vipt-eng.html>

FIGURE 3

Share of Building Canada Fund by Province and Territory



Source: Data from Infrastructure Canada and Statistics Canada

In theory, base funding is a type of need-based approach, recognizing that very small jurisdictions (of which Canada has its share) may have costs that are disproportionate to their ability to raise revenue. However, the equal per jurisdiction approach is so crude and divorced from any actual measure of need that it cannot fairly be called need-based. The result is simply a formula that gives a major advantage to smaller and less populous provinces at the expense of larger ones.

Base funding carve outs are far out of keeping with the policy rationale of the infrastructure program. There is no clear case that infrastructure needs are relatively greater in smaller provinces. Quite the contrary, Canada’s largest cities have needs for transit and other infrastructure investments that make urban economies run smoothly. Ultimately, base funding comes at the expense of transit investments in Canada’s largest city-regions like Montreal, Toronto, and Vancouver, increasing congestion and undermining economic growth.

The renewed Building Canada Fund unfortunately carves out an even larger share of the funding total for equal-per-jurisdiction base funding than in the previous version of the program (up from about one quarter to about one third). For Ontario, this means a declining share of federal infrastructure funding and just under \$1B less funding over the course of the program than the province would receive without this carve out. Not only did the federal government not redress the unprincipled allocation, they made it worse, with no justification or explanation.

Unclear rationale for ‘Merit-based’ Infrastructure spending

Other major components of federal infrastructure funding are allocated on a merit basis. The way these eligibility requirements are designed has a major bearing on how this infrastructure support gets distributed throughout the country. Take the cases of the Green Infrastructure Fund (a \$1B fund announced as part of the Economic Action Plan), the Strategic Infrastructure Fund (\$4.3B over 9 years through 2012-13) and the Public-Private-Partnerships Fund (a \$1.25B component of the 2007 Building Canada Plan).

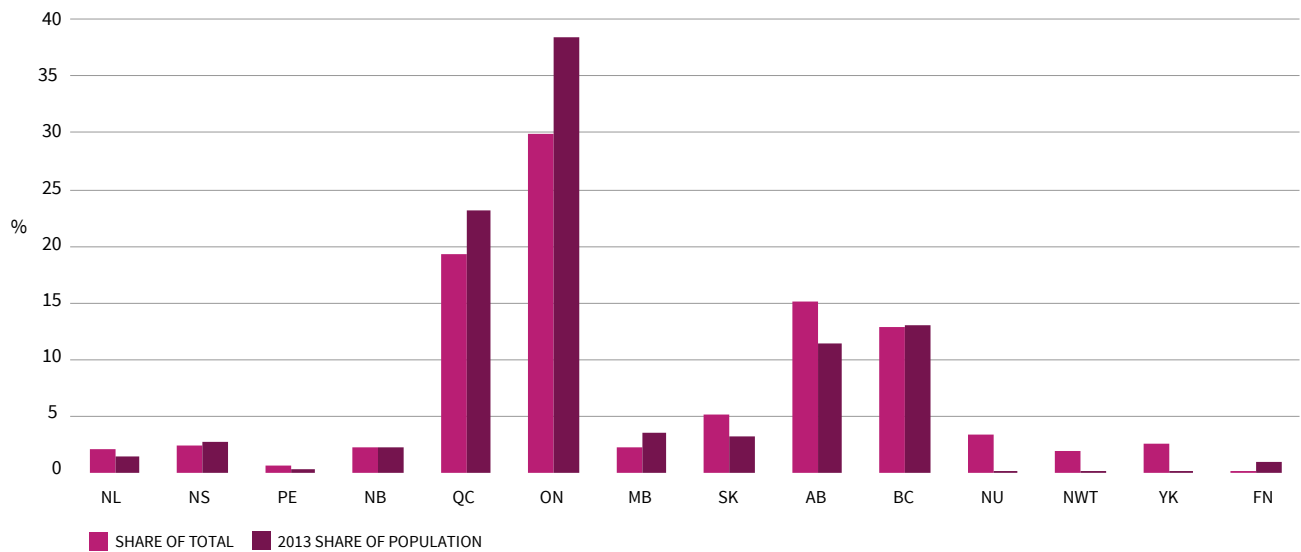
Each of these programs has broad merit-based criteria on the surface—but there are significant differences in how provinces and territories have been able to access the funding. To make matters even less transparent, barely two thirds of the Green Infrastructure Fund has been allocated to projects publicly listed under the fund, with \$215M transferred to other federal departments and a further \$146M not publicly accounted for.²⁵ Oft-delayed release by the federal government of these criteria also poses a challenge for provincial or local governments that would otherwise make applications on the basis of merit.

25 Mowat Centre analysis based on project listing here. <http://www.infrastructure.gc.ca/prog/gif-fiv-eng.html>

26 Figures from Infrastructure Canada. <http://www.infrastructure.gc.ca/prog/index-eng.html>. 1/3rd shares represent the Northern Indigenous Community Satellite Network in MB, QC, and ON funded through the Strategic Infrastructure Fund.

FIGURE 4

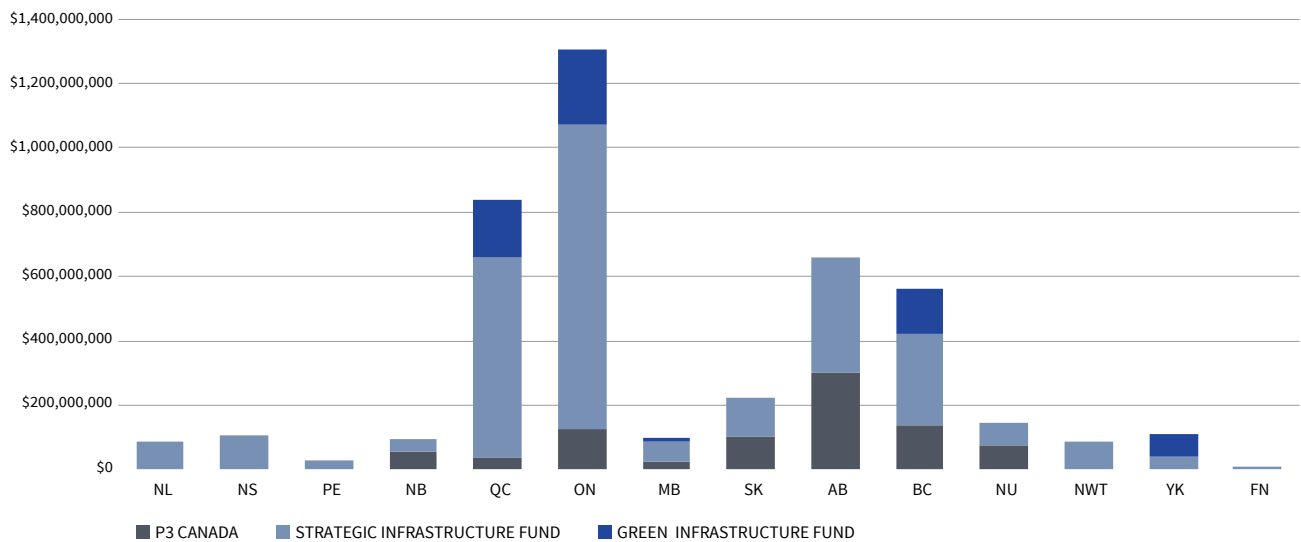
Share of Green Infrastructure Fund, Strategic Infrastructure Fund and P3 Canada Fund²⁶



Source: Data from Infrastructure Canada and Statistics Canada

FIGURE 5

Merit-Based Infrastructure Funding Allocation



Source: Data from Infrastructure Canada and Statistics Canada

Unsurprisingly, Ontario fares quite poorly under the vague and non-transparent ‘merit-based’ allocation from these infrastructure funds, benefitting from only 30 per cent of the federal investments from these three funds compared to 38.5 per cent of the national population. This includes a mere 14 per cent of the funding under the P3 Canada fund, despite Ontario having a well developed industry for delivering infrastructure through public-private partnerships, particularly through Infrastructure Ontario. Alberta, on the other hand, receives far more than its per capita share. These results raise questions about how these programs are designed and how ‘merit’ is being determined.

Infrastructure Stimulus Fund

In their January 2009 budget, the federal government announced a \$4B Infrastructure Stimulus Fund as a centerpiece of its response to the recession. Transfers to provinces and territories, municipalities, and non-profit organizations would be used to match investments across a range of infrastructure categories. In a positive step, the budget announcement provided at least some description of how the funding would be allocated, saying:

“subject to project readiness and merit, funding will be allocated for projects in provinces and territories based on their population. Should agreements not be reached expeditiously with a province or territory, funding may be used to support the rehabilitation of federal or other infrastructure.”²⁷

This commitment acknowledged the basic intention for how this \$4B in spending would be allocated, even if too vague to support accountability. As the table below demonstrates, the best available data shows that the allocation in practice was largely consistent with this objective. Unfortunately, piecing together this largely positive picture is obscured by the lack of reporting and available data. Without the Parliamentary Budget Officer’s efforts, one would have to synthesize information from each of the 4000 projects over two years of public accounts data. Canadians would be much better served by clear, accessible and proactive disclosure from the federal government directly.

The Gas Tax Fund

The Gas Tax fund, worth \$2B annually in 2014-15 and set to grow to \$2.2B annually by 2018-19, allocates revenues from federal excise taxes on gasoline to municipalities, based on agreements with provinces and territories. The funding is allocated mostly on a per capita basis with some minimum base amounts carved out for PEI and the territories based on their size.²⁹ The funding is conditional on municipalities using the money for eligible project types. Within provinces, funding typically goes to municipalities on a per capita basis, with the exception of BC, which has developed an alternative three-tier approach.³⁰

FIGURE 6
Infrastructure Stimulus Fund Allocations

PROVINCE/ TERRITORY	APPLICATIONS	FEDERAL CONTRIBUTION	SHARE OF TOTAL TRANSFER	SHARE OF 2010 POPULATION
NL	28	\$59,069,525	1.6%	1.5%
PE	18	\$16,008,105	0.4%	0.4%
NS	109	\$98,528,416	2.7%	2.8%
NB	50	\$90,964,434	2.5%	2.2%
QC	863	\$836,951,591	22.9%	23.3%
ON	1923	\$1,408,896,055	38.5%	38.6%
MB	111	\$143,016,395	3.9%	3.6%
SK	150	\$115,437,263	3.2%	3.1%
AB	235	\$411,328,670	11.2%	11.0%
BC	389	\$470,120,911	12.8%	13.1%
NU	2	\$3,558,740	0.1%	0.1%
NWT	21	\$4,986,000	0.1%	0.1%
YK	14	\$3,825,419	0.1%	0.1%
Total	3913	\$3,662,691,525		

Source: Data Compiled by Parliamentary Budget Office²⁸

27 Finance Canada. *Budget 2009*. pg. 146 <http://www.budget.gc.ca/2009/pdf/budget-planbugetaire-eng.pdf>

28 This data compiled by the Parliamentary Budget Officer is the most recent and complete accounting available, but does not represent a final accounting of how the z was allocated. *Infrastructure Stimulus Fund Applications and Claims*. August 2010. http://www.pbo-dpb.gc.ca/files/get/resources/65?path=%2Ffiles%2Ffiles%2FResearch+Resources%2FR3-ISF-+application+and+claims_FSI-demandes+et+r%C3%A9clamations.xlsx

29 Infrastructure Canada.

30 Union of BC Municipalities. <http://www.ubcm.ca/EN/main/funding/gas-tax-fund.html>
31 Funding allocations from Infrastructure Canada, Population share based on Statistics Canada Table 051-0001 Estimates of population, by age group and sex for July 1, Canada, provinces and territories, annual (persons)(1,2,6,7). First Nations Share of Population based on share living On Reserve as funding is allocated to First Nations governments <http://www12.statcan.gc.ca/nhs-enm/2011/as-sa/99-011-x/2011001/tbl/tbl03-eng.cfm>

FIGURE 7
Gas Tax Funding Allocation by Province³¹

JURISDICTION	2014-15 FUNDING \$ (THOUSANDS)	SHARE OF 2014-15 FUNDING	2013 SHARE OF POPULATION
Newfoundland and Labrador	\$29,865	1.5%	1.5%
Prince Edward Island	\$15,000	0.8%	0.4%
Nova Scotia	\$53,226	2.7%	2.7%
New Brunswick	\$43,322	2.2%	2.2%
Quebec	\$458,219	22.9%	23.2%
Ontario	\$744,949	37.2%	38.5%
Manitoba	\$65,471	3.3%	3.5%
Saskatchewan	\$56,290	2.8%	3.2%
Alberta	\$208,651	10.4%	11.4%
British Columbia	\$253,277	12.7%	13.0%
Yukon	\$15,000	0.8%	0.1%
Northwest Territories	\$15,000	0.8%	0.1%
Nunavut	\$15,000	0.8%	0.1%
First Nations	\$26,731	1.3%	0.9%
Total	\$2,000,000		

Source: Data from Infrastructure Canada and Statistics Canada

Labour Market Training

Federal Funding for Active Employment Measures

Active employment measures include a range of programs aimed at connecting people to employment, whether by supporting skills development, helping individuals in their job search, or providing wage subsidies or other supports to create employment opportunities. The federal government provides almost \$2.5B in funding annually for “active employment measures” for the broader working population (excluding separate funding agreements for people with disabilities) through programs delivered by provinces and territories.

Federal funding to provinces and territories for active employment measures comes through two different streams. The Labour Market Development Agreements cover programs funded through Part II of the *Employment Insurance Act*, limiting eligibility to those that qualify for EI benefits. Recognizing the increasing number of Canadian workers left out of the EI umbrella in the mid 2000s, the federal government introduced a complementary pool of funding in the Labour Market Agreements, aimed at helping

Canadians underrepresented in the labour force (especially unemployed workers that are not eligible for EI).

Despite being targeted at a specific population, the federal government opted for a per capita funding approach for the Labour Market Agreements, rather than an equal per client approach that would naturally flow from the objectives of the program. No explanation was given for why an equal per capita approach was appropriate in these circumstances.

Because design and delivery of all of these programs has been devolved to provinces and territories over the course of the past 20 years, this funding is provided in annual block grants to provincial and territorial governments. Beginning this year however, the federal government has reversed this trend with the Canada Job Grant, which carves out a major chunk of existing transfers to fund a new federal program.³²

This is a program with a clearly identified client group that is tracked in a consistent way. The most appropriate allocation for federal funding for active employment measures would be on an equal per client basis. Barring that, another reasonable approach would be to distribute funding on an equal per capita basis.

In reality, federal funding for active employment measures is skewed by both historical legacies and current distortions in the EI program. The result is a non-transparent approach to funding that punishes Canadians living in Ontario and in Alberta, provinces that receive far less than their share of the population or of Canada’s unemployed would dictate (see figure 8 for details). The driver of this inequity is the Labour Market Development Agreements which allocate only 29 per cent of funding to Ontario and 5.6 per cent to Alberta, rather than the newer Labour Market Agreements, which are distributed on an equal per capita basis.

It is worth noting that the Labour Market Agreements first originated from an attempt to make up for the distortions in Labour Market Development Agreements which punished Ontario. As the figure below shows, when these agreements were ultimately expanded throughout the country the allocation returned to one that is skewed heavily against Ontario—a condition that persists today.

³² For more on the Canada Job Grant, see Mendelson and Zon, 2013. *The Training Wheels Are Off: A Closer Look at the Canada Job Grant*. <http://mowatcentre.ca/the-training-wheels-are-off/>

³³ Funding totals based on planned Federal 2013 expenditures (LMDA totals are based on EI Part II expenditure plan). Population shares from Statistics Canada, Share of Canada’s Unemployed based on 5 year rolling average from Statistics Canada Labour Force Survey.

Improving this situation does not need to be complicated. The Mowat Centre Employment Insurance Task Force recommended a new single transfer to provinces for unemployed persons (including the Labour Market Agreement for Persons with Disabilities), conditional on the overall objectives of the program and allocated on a per client basis—the province’s share of unemployed persons.³⁴ This recommendation remains a sensible approach to a more principled allocation of federal funding for active employment measures, given that the hodgepodge of transfers with different allocation formula has resulted in funding for training dollars that follows no recognizable principle.

Labour Market Agreements for Persons with Disabilities

The Labour Market Agreements for Persons with Disabilities (LMA PD) provides \$218M annually to provinces for employment supports and training to persons with disabilities. The types of supports funded through these agreements range from employment counselling to technical aids to wage subsidies.³⁵ The allocation among provinces is not based on per capita, per client or expenditure need. Instead it builds on a legacy of historical commitments which include base funding and per capita portions that are frozen in time from over a decade ago.

FIGURE 8
Federal Funding for Active Employment Measures³³

PT	LABOUR MARKET AGREEMENTS	LABOUR MARKET DEVELOPMENT AGREEMENTS	TOTAL	SHARE OF TOTAL	2013 POPULATION SHARE	SHARE OF CANADA'S UNEMPLOYED
NL	\$7,349,000	\$129,219,000	\$136,568,000	5.6%	1.5%	2.6%
PE	\$2,094,000	\$26,084,000	\$28,178,000	1.2%	0.4%	0.7%
NS	\$13,599,000	\$79,014,000	\$92,613,000	3.8%	2.7%	3.2%
NB	\$10,836,000	\$89,763,000	\$100,599,000	4.1%	2.2%	2.7%
QC	\$115,462,000	\$581,242,000	\$696,704,000	28.4%	23.2%	24.3%
ON	\$193,603,000	\$565,471,000	\$759,074,000	31.0%	38.5%	42.1%
MB	\$18,162,000	\$43,507,000	\$61,669,000	2.5%	3.5%	2.4%
SK	\$15,481,000	\$36,426,000	\$51,907,000	2.1%	3.2%	1.9%
AB	\$55,529,000	\$109,143,000	\$164,672,000	6.7%	11.4%	8.5%
BC	\$66,263,000	\$280,647,000	\$346,910,000	14.2%	13.0%	12.1%
NU	\$483,000	\$2,859,000	\$3,342,000	0.1%	0.1%	0.1%
NWT	\$621,000	\$3,143,000	\$3,764,000	0.2%	0.1%	0.1%
YK	\$518,000	\$3,482,000	\$4,000,000	0.2%	0.1%	0.1%
Total	\$500,000,000	\$1,950,000,000	\$2,450,000,000			

Source: Data from Employment and Social Development Canada and Statistics Canada

34 Mowat Centre Employment Insurance Task Force. 2011. *Making it Work: Final Recommendations of the Mowat Centre Employment Insurance Task Force*. pg. 56.

35 Employment and Social Development Canada. http://www.esdc.gc.ca/eng/jobs/training_agreements/lma_disabilities/index.shtml

FIGURE 9
Funding for Labour Market Agreements for Persons with Disabilities by Province

PROVINCE	FUNDING	SHARE OF FUNDING	SHARE OF POPULATION (2013)
NL	\$4,578,367	2.1%	1.5%
PEI	\$1,375,659	0.6%	0.4%
NS	\$8,290,346	3.8%	2.7%
NB	\$5,958,848	2.7%	2.2%
QC	\$45,892,915	21.0%	23.2%
ON	\$76,411,477	35.0%	38.5%
MB	\$8,964,971	4.1%	3.5%
SK	\$10,852,608	5.0%	3.2%
AB	\$25,190,332	11.5%	11.4%
BC	\$30,744,084	14.1%	13.0%

Source: Data from Employment and Social Development Canada and Statistics Canada

The federal government announced the renewal of the LMAPD agreements in 2014, as the federal government is interested in introducing a new generation of agreements that will better connect individuals in need to potential employers.³⁶ The federal government should take this opportunity to move to a per capita or per client approach that better ensures that Canadians are treated fairly regardless of where they live. This should include renewing or replacing a strong source of information on where Canadians with disabilities live, which was formerly available through the Statistics Canada Participation and Activity Limitation Survey (now discontinued).

Immigrant Settlement Funding

While immigration is an area of concurrent federal and provincial jurisdiction, the federal government has always been the predominant actor in Canada. This applies both to decisions on who may enter the country and become Canadian as well as the services and supports to assist newcomers with settlement and integration.

The Settlement Funding Formula (SFF) dictates the amount that the federal government allocates for immigrant settlement programs in provinces outside of Quebec. The SFF is advertised as an equal-per-client approach, allocating an equal amount for each immigrant to each province or territory, with higher amounts for each refugee given their increased service needs.³⁷ In practice however there are a number of deviations from this principled approach hidden within the formula. Funding totals include an unspecified “capacity amount” per province, and \$16M set aside for a national “innovation fund” with guidelines not made clear publicly.

Further skewing the allocation picture for immigrant settlement funding is the fact that in 1991 the Government of Quebec secured an agreement from the federal government that not only accorded the province unique decision-making authority in the selection of immigrants to the province, but also gave Quebec its own formula for federal settlement funds that has far exceeded the amount received per immigrant (or per capita) by other provinces.³⁸ This legacy agreement, signed at a time when Canada’s immigration system and settlement services were managed very differently, has a significant influence on the distribution of settlement funds, moving it away from the principles expressed in the SFF.

³⁶ Government of Canada. <http://actionplan.gc.ca/en/initiative/reforming-labour-market-agreements-persons>

³⁷ Citizenship and Immigration Canada, 2011. <http://www.cic.gc.ca/english/department/media/backgrounders/2011/2011-11-25.asp>

³⁸ The Canada-Quebec Accord can be found here: <http://www.cic.gc.ca/english/department/laws-policy/agreements/quebec/can-que.asp>

THE BIGGER PICTURE

Allocation Decisions in Federal Spending

The examples in this paper cover the more direct and measurable cases of the way allocation approaches for federal transfers shape the realities of our federation. But there are also more indirect and harder to track regional dimensions of federal spending allocation that also have significant influence on the way our federal system shapes the public services available to Canadians.

Some federal investments are not presented as part of a broader program, making it difficult to evaluate their regional distribution. For example, the federal government's loan guarantee for the Lower Churchill hydro development was situated in a Speech from the Throne commitment to "support major new clean energy projects of national or regional significance"⁴¹, making it impossible to make a clear comparison for regional equity. This is similarly true for support for the auto sector almost entirely based in Ontario.

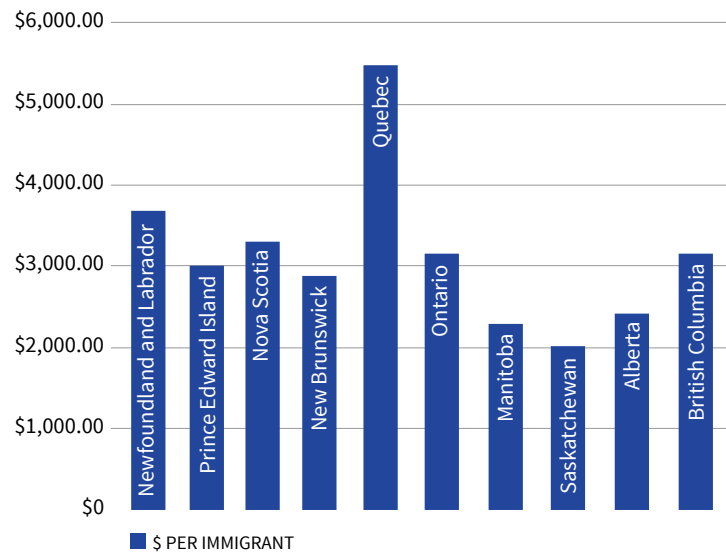
Where direct comparisons are possible, it can reveal significant unexplained distortions in how federal spending is allocated on a regional basis. Looking at federal support for regional economic development agencies, there is no clear basis for the relative levels of investment beyond historical timing and political decision-making.

To begin with, some Canadian regions have consistently had dedicated independent economic development agencies since the late 1980's while others have fallen within the general responsibility of the Department of Industry.⁴² To further complicate matters, these different organizations do not have congruent mandates and publish little information about their own mandates.

While these funds (see Figure 12) don't neatly fit the picture of federal transfer payments being allocated, they nonetheless influence the shape of regional redistribution in Canada. The federal government should more clearly explain how decisions are made on regional allocation of investments in economic development, energy or any other areas of federal spending with a regional dimension. It is possible there is a rationale but it is not apparent or articulated.

Before the establishment of dedicated regional economic development funds in the 1980's, the federal government had a more principled need-based allocation approach that took into account employment and other economic trends. These lessons are worth considering to bring clarity and

FIGURE 10
Federal Settlement Funding Ranges Significantly³⁹



Source: Data from Citizenship and Immigration Canada

FIGURE 11
Immigrant Settlement Funding in 2012-13⁴⁰

JURISDICTION	2012-13 FUNDING	SHARE OF 2012-13 FUNDING	SHARE OF 2011 IMMIGRANTS	FUNDING PER IMMIGRANT
Newfoundland and Labrador	\$2,512,975	0.29%	0.27%	\$3,684.71
Prince Edward Island	\$5,218,024	0.61%	0.70%	\$3,014.46
Nova Scotia	\$7,078,944	0.82%	0.86%	\$3,311.01
New Brunswick	\$5,664,069	0.66%	0.79%	\$2,879.55
Quebec	\$283,100,000	32.92%	20.80%	\$5,470.95
Ontario	\$314,950,874	36.62%	39.98%	\$3,166.67
Manitoba	\$36,539,512	4.25%	6.42%	\$2,289.01
Saskatchewan	\$17,995,061	2.09%	3.60%	\$2,009.50
Alberta	\$74,978,539	8.72%	12.45%	\$2,421.71
British Columbia	\$109,813,233	12.77%	13.98%	\$3,156.73
Yukon	\$723,998	0.08%	0.03%	\$8,517.62
Northwest Territories	\$469,800	0.05%	0.01%	\$19,575.00
Nunavut	\$932,632	0.11%	0.10%	\$3,935.16

Source: Data from Citizenship and Immigration Canada

41 Speech from the Throne, 2011. http://www.speech.gc.ca/lo-cal_grfx/docs/sft-ddt-2011_e.pdf

42 Dupuis, 2011. <http://www.parl.gc.ca/content/lop/researchpublications/2011-05-e.htm>. For further analysis of overlapping and difficult to track investments in economic development in Canada, see the 2013 Mowat Centre publication *Let's Talk: Coordinating Economic Development Spending in Canada*. <http://mowatcentre.ca/lets-talk/>

39 Data from Citizenship and Immigration Canada. Territories excluded from this chart as their higher rate per immigrant recognize their unique circumstances for service delivery.

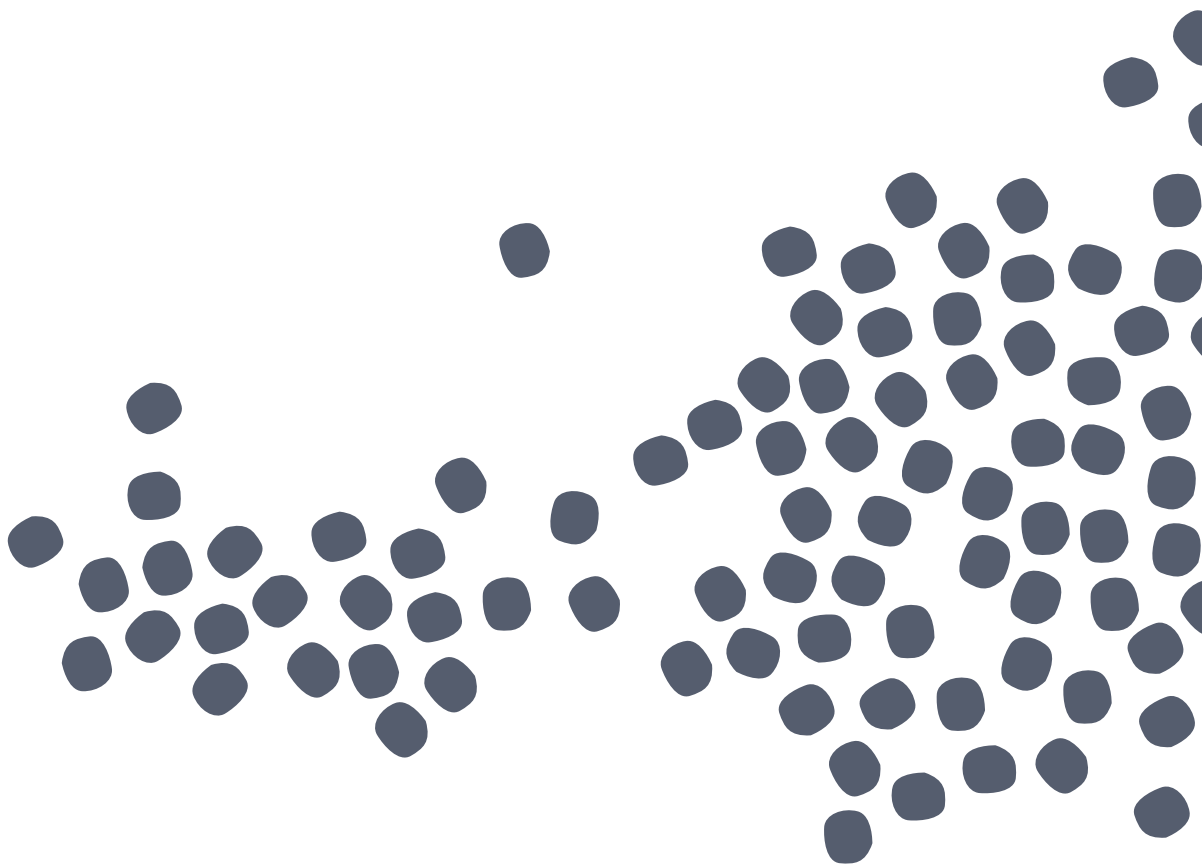
40 Data from Citizenship and Immigration Canada, <http://www.cic.gc.ca/english/department/media/backgrounders/2011/2011-11-25.asp>; <http://www.cic.gc.ca/english/resources/statistics/facts2012/permanent/12.asp>; <http://www.cic.gc.ca/english/resources/statistics/facts2012/permanent/11.asp>

FIGURE 12

Federal Regional Economic Development Agency Funding⁴³

PROGRAM/AGENCY	2013-14 FUNDING	SHARE OF DEDICATED REGIONAL ECONOMIC DEVELOPMENT FUNDING	SHARE OF 2013 POPULATION
Atlantic Canada Opportunities Agency	\$300M	25.4%	6.8%
Enterprise Cape Breton Corporation	\$51.8M	4.4%	0.3%
Economic Development Agency of Canada for the Regions of Quebec	\$254.9M	21.6%	23.2%
Federal Economic Development Agency for Southern Ontario	\$222.8M	29.1%	38.5%
FedNor Economic Development Initiative (Northern Ontario)	\$120.7M		
Western Economic Diversification	\$178.7M	15.1%	30.8%
Canadian Northern Economic Development Agency	\$51.8M	4.4%	0.3%
Total Dedicated Regional Economic Development Funding	\$1180.7M		

Source: Data from Treasury Board of Canada 2013-14 Main Estimates and Statistics Canada



⁴³ Figures come from 2013-14 Main Estimates <http://www.tbs-sct.gc.ca/ems-sgd/20132014/me-bpd/me-bpd02-eng.asp> except for FedNor, whose budget is not clearly identified in federal budget documents. FedNor figures are based on assessment by David Akin. <http://blogs.canoe.ca/davidakin/main-page/mulcair-clement-clash-on-fednor-funding/>

5 Conclusion and Recommendations

Each year, the federal government collects and redistributes over \$160B in tax dollars across the country. Each transfer is usually debated on its policy merits, but the regional dimension of transfers is rarely discussed outside of the Equalization program.

In Canada, where regional grievances can be easily mobilized, the opaque nature of many transfers make it all too easy for provincial voices to complain—and for the federal government to dismiss these complaints as mere whining. But some of the complaints have merit, and the federal government bears a good deal of responsibility for the complaints because allocation approaches are too often unclear and unprincipled.

It is reasonable for Canadians to expect that the way transfers are allocated would be rooted in consistent and clearly stated principles. In a number of cases, this is true of federal transfers. However, as the examples in this report illustrate, there is considerable room for improvement. This is particularly true for Ontario, which more than any other province consistently receives less than one would expect if a principled allocation was used. When added together, these contribute to a significant shortfall in federal spending in Ontario, which the Mowat Centre explored in *Filling the Gap: Measuring Ontario's Balance with the Federation*.⁴⁴

The first step to rectifying this situation is agreement upon a core set of principles. As a starting place we propose four:

1. The allocation approach should be clear, transparent and understandable to Canadians
2. The approach should treat Canadians fairly, regardless of where they live
3. The approach should be consistent with the policy objectives of the transfer
4. The approach should be provide predictability, but update when circumstances change

These principles serve the interests of Canadians and their governments at all levels. They are flexible enough to leave room for a variety of allocation approaches, depending on

the circumstances. In particular, equal per capita, equal per client, need-based and merit-based approaches all have the potential to embody these principles in the right circumstances.

An essential ingredient for reform is improved transparency. The federal government should clearly and proactively explain to Canadians how regional allocation decisions are made for federal transfers and the principles upon which they are based, and should provide the appropriate spending information so that Canadians can judge for themselves how well each case meets these principles. These explanations should be front and centre in communication and briefing products released publicly when the federal government makes announcements on programs and transfers. The Canada Health Transfer and Canada Social Transfer are reasonably good examples to build on: each is clearly allocated on an equal per capita approach and each province or territory's funding is published. The federal government should build on this effort and expand it to the full range of transfers.

The federal government should clearly and proactively explain to Canadians how regional allocation decisions are made for federal transfers

With firm principles and increased transparency, the final step is to correct the distortions that diverge from principled allocations. Where there are good reasons to maintain the status quo, that explanation should be clearly provided to Canadians. For many, those explanations have not been forthcoming.

Many federal-provincial transfers have quietly entered periods of transition and renewal. Labour market training and infrastructure programs are currently being negotiated between federal and provincial governments. The federal government should seize this opportunity to adopt a clear, transparent, and principled approach to the allocation of transfers.

⁴⁴ Zon, 2013. *Filling the Gap: Measuring Ontario's Balance with the Federation*. <http://mowatcentre.ca/filling-the-gap/>

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