Budget Paper D

UPDATE ON FISCAL ARRANGEMENTS: FEDERAL ACTIONS IMPACTING MANITOBA

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Manitoba

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Manitobans expect there to be a strong partnership between the provincial government and the federal government that supports growth and development in the province, while protecting the services families rely on.

Since 2006, the federal government has taken actions that are impacting individual Manitobans and the province overall. These include: reductions in direct federal program expenditures; reductions to federal transfers; the introduction of new programs that require provincial cost-sharing or other incremental provincial funding; and other changes to federal policies and regulations.

Transfers to Manitoba

Fiscal arrangements are an important aspect of the partnership between the federal government and the provinces and territories. About two-thirds of total federal program spending is designated for transfers. This includes transfers to other levels of government, primarily through major transfers to provinces and territories, as well as transfers to individuals.

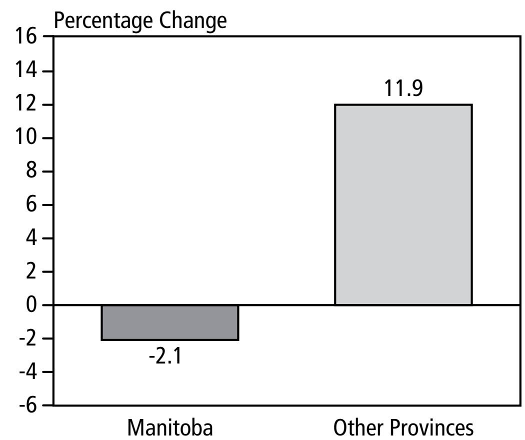
Every province and territory receives transfer payments to fund the delivery of essential services, such as health care and education, and for a variety of other priorities including infrastructure and labour market development. Stable and adequate federal transfer payments help the province to stimulate the economy and drive growth through investments in both physical and human capital.

Unfortunately, while federal transfers have continued to increase on a national level, growth in transfers to Manitoba has been lackluster in comparison. From 2009/10 to 2013/14 total federal transfers to Manitoba have fallen by 2.1% compared to growth of 11.9% to the other provinces overall. As a share of Manitoba's total revenue, federal transfers have fallen steadily since 2009/10. When inflation and population growth is taken into account, the real value of transfers to Manitoba is lower now than it was in 2006/07.

Major federal transfers, including the Canada Health Transfer (CHT), Canada Social Transfer (CST) and Equalization, make up about 90% of total federal transfers to Manitoba. When the federal government changes these programs, the impacts are significant. Since 2006, the federal government has made several changes to the major transfers that are having a negative impact on Manitoba.

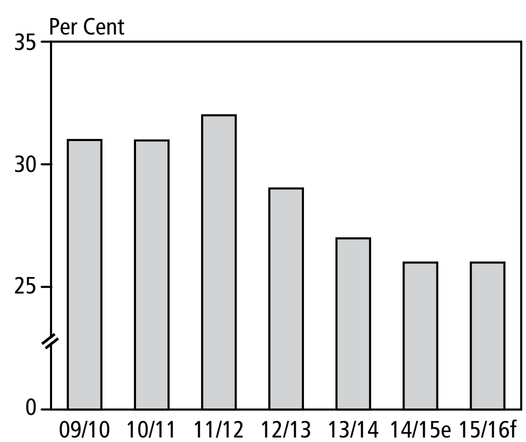
In November 2008, the federal government announced its decision to change the Equalization Program, limiting its growth to no more than the growth in Canada's nominal GDP. As a result, the program is no longer meeting its objectives, as the constrained program no longer ensures provinces are raised to the national average. This decision has reduced total Equalization payments to receiving provinces by almost $21 billion from 2009/10 to 2015/16. Fortunately, since the introduction of these changes, Manitoba's

Growth in Total Federal Transfers, 2009/10 to 2013/14



Source: Provincial Public Accounts

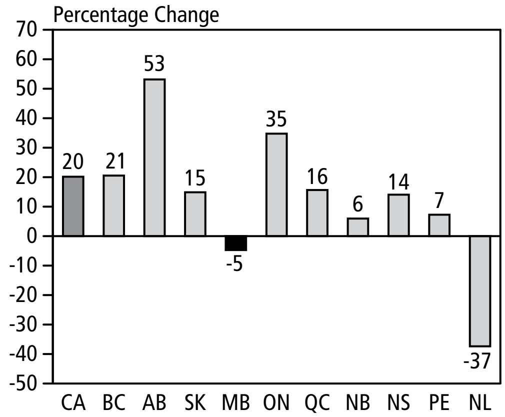
Total Federal Transfers to Manitoba as a Share of Total Provincial Revenue



f - Forecast e - Estimate

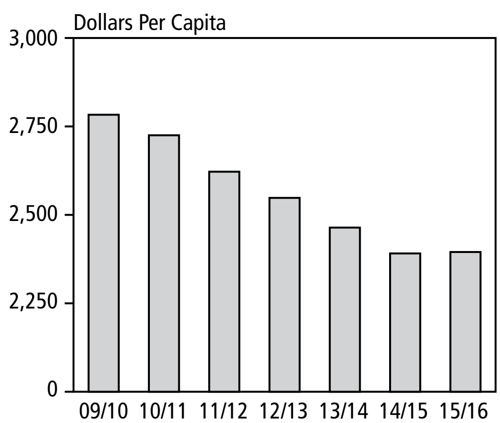
Sources: Finance Canada and Manitoba Finance

Growth in Per Capita Major Transfers, 2009/10 to 2015/16



Source: Finance Canada

Real, Per Capita Major Transfers to Manitoba, 2009 Dollars



Sources: Finance Canada and Manitoba Finance

losses were partially offset by federal Total Transfer Protection, an initiative that was discontinued after 2013/14. Since 2013/14, the growth limit on the program has reduced Manitoba's Equalization entitlements by $84 million in 2014/15 and $91 million in 2015/16.

Due to another unilateral decision, the federal government's contribution to health care in Canada will be reduced by about $26 billion from 2017/18 to 2023/24. Beginning in 2017/18, the annual CHT escalator will fall from 6% to the rate of growth of nominal GDP. Limiting the rate of growth in the CHT will improve the federal government's fiscal situation, but it will come at the expense of provinces and territories, which must address health care cost pressures resulting from population ageing and growth as well as the ongoing demands for innovation and program improvements.

With medium- and long-term health care costs likely growing at a rate above nominal GDP (the Office of the Parliamentary Budget Officer's Fiscal Sustainability Report 2014 estimated provincial-territorial health spending will increase by 4.8% annually from 2013 to 2050), the federal share of aggregate provincial-territorial health expenditures is expected to fall from about 20% currently to about 17% or 18% by 2035.

With the CST annual escalator set below the rate of projected nominal GDP growth, CST related spending as a share of the economy will gradually decline over time. The 3% annual CST growth escalator is also below the projected growth rate of provincial and territorial spending on social programs and post-secondary education.

In its 2007 Budget, the federal government announced that it would move to an equal per capita cash allocation for the CHT and CST, leaving Equalization as the only major federal transfer program that takes into account differences in provincial revenue-raising capacity.

When the CST moved to an equal per capita cash allocation in 2007/08, the federal government committed that no province or territory would receive less under an equal per capita allocation than it would have under the previous system. Accordingly, the federal government provided an additional $687 million in 2007/08 to offset the impact on affected jurisdictions. Provinces and territories were promised similar transition protection when the CHT moved to an equal per capita cash allocation in 2014/15.

However, when the CHT was changed to an equal per capita allocation in 2014/15, the full transition protection committed to by the federal government in Budget 2007 was not provided. Manitoba estimates its loss due to the limited protection was $31 million in 2014/15, and will be about $350 million from 2015/16 to 2023/24.

Others Actions

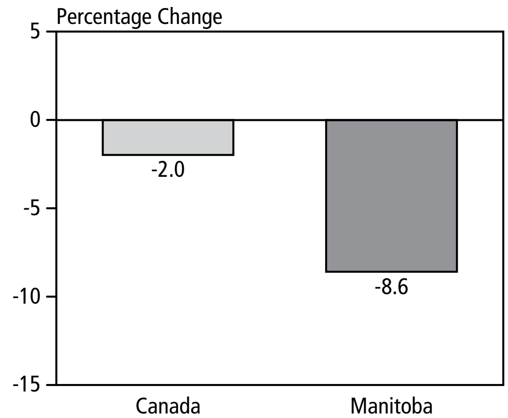
Stalled growth in federal funding to Manitoba and a reduced federal presence in the province is affecting Manitobans. Manitoba understands that governments must be fiscally responsible. However, decisions by all levels of government must take into account the need to ensure citizens continue to have access to vital public services.

As part of its efforts to balance its budget, the federal government has been pursuing spending and staffing reductions, and Manitoba has seen more than its fair share of these cuts. In 2014, there were almost 9% fewer federal government employees working in Manitoba than there were in 2006. This compares to an overall reduction of 2% in the rest of Canada over the same period.

The province is concerned that these ongoing and disproportionate cuts are resulting in an erosion of the quality and accessibility of programs and services for Manitobans and placing pressure on the province to address gaps. For example, Manitobans now have less access to walk-in services at Canada Revenue Agency offices.

Other key services, such as those offered by Statistics Canada, have been particularly impacted by federal actions and Manitoba is concerned that these cuts are not only impacting transfers, they are also reducing our access to quality data and information for planning and program development.

Reduction in the Number of Federal Government Employees, 2006 to 2014



Source: Statistics Canada, Survey of Employment, Payroll and Hours

On September 26, 2013, Statistics Canada released new population estimates based on the final results of Census 2011. Manitoba's population was revised down by almost 18,000 persons compared to pre-Census 2011 estimates. Manitoba Bureau of Statistics (MBS) has indicated there are significant problems with the methodology used by Statistics Canada in determining Manitoba's final population count under Census 2011.

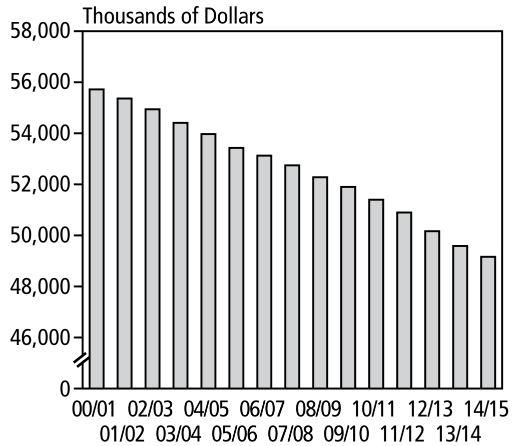
As most federal transfer programs use population in their calculations, this questionable downward revision continues to have a negative financial impact on the province. Manitoba expects it will lose about $100 million annually, or about a half-billion dollars overall, before the next census is completed and new population estimates are released in 2018.

Federal actions will also directly impact individual Manitobans. Recently, the federal government decided it will increase the eligibility age for Old Age Security (OAS) and the Guaranteed Income Supplement (GIS) by two years, from 65 to 67. The sharp decline in poverty among Canada's seniors is largely attributed to improvements in OAS during the 1970's and 1980's. Canada now has one of the lowest senior poverty rates in the world. Manitoba is concerned these changes will have a material impact on seniors, particularly lower-income seniors.

The federal government claims the OAS changes are necessary to ensure the sustainability of the program. However, the Parliamentary Budget Office (PBO) has considered the issue and concluded in a 2012 report that there is no fiscal reason to raise the OAS eligibility age, and that the program could actually be enhanced without putting the federal government's long-term fiscal sustainability at risk (Source: PBO, Federal Fiscal Sustainability and Elderly Benefits, February 8, 2012).

In order to improve its bottom line, the federal government has frozen Employment Insurance (EI) premium rates for 2015 and 2016 at the higher than necessary level of $1.88 per $100 of insurable earnings. According to the Office of the Chief Actuary, the rate required to cover the expenses of the EI Program is much lower. (Source: 2015 Actuarial Report on the EI Premium Rate).

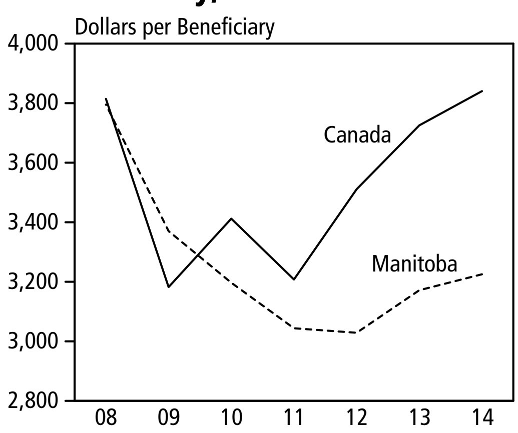
Manitoba's LMDA Allocation since 2000/01



Note: This includes the funds transferred to Manitoba to help cover administrative costs related to the LMDAs, but does not include the additional $23.1 million in federal one-time "stimulus" funding provided over two years (2009/10 and 2010/11).

Source: Government of Canada

LMDA Allocation Per Regular EI Beneficiary, 2008 to 2014



Note: Includes the additional federal "stimulus" funding provided in 2009/10 and 2010/11. Excludes funds to cover administrative costs.

Sources: Government of Canada; Statistics Canada

Unnecessarily high EI premium rates (above and beyond what is required to balance the EI Operating Account) helped the federal government to balance its budget early by reducing its deficit by an estimated $1.8 billion in 2015. In 2016, the federal government estimates that excess EI contributions will provide another $3.8 billion to its bottom line, bringing the EI Operating Account surplus to $5.5 billion (Federal Budget 2015).

Because Manitoba is a "net contributor" to the EI Program, due primarily to its below-average unemployment rate, this is another good example of how Manitoba is being disproportionally impacted by a federal government action.

These actions by the federal government also come at a time when fewer and fewer unemployed workers are able to access the EI Program. Unfortunately, the federal government has not made corresponding adjustments to EI to accommodate the realities of a changing labour market. The surplus EI contributions that will be created due to the rate freeze could be used to extend access to the EI Program to more workers, increase income benefits, or enhance skills training provided through the Labour Market Development Agreements (LMDA).

Every year since 2000/01, the federal government has allocated a fixed $1.95 billion in program funding from the EI Account to the provinces and territories under the LMDA to support skills training and other labour market programs and services. LMDA program funding is allocated to provinces and territories based on a complicated "17 variable" formula. Manitoba's allocation has declined by about half a million dollars every year, representing a cumulative loss of $50 million for Manitoba since 2000/01.

Manitoba appreciates the additional LMDA funding provided to all provinces and territories in 2009/10 and 2010/11. Unfortunately, the funding was time-limited and was not enough to keep up with the increased need for skills training in response to the recession.

Since that time, and despite an improvement in the economy and labour market, Manitoba's capacity to meet ongoing demand for skills training through the LMDA remains well below pre-recession levels. For example, once adjusted for the number of regular EI beneficiaries, Manitoba now has almost $600 less LMDA funding per potential trainee than it did in 2008. In contrast, the average amount available across Canada is now higher than it was in 2008.

In addition to some of these more prominent examples, federal actions are having a negative impact in many other areas. The Appendix presents examples from across government departments of federal actions that are impacting Manitobans. In several of these examples it is evident that provinces and territories have had to react to ensure citizens continue to have access to needed programs and services.

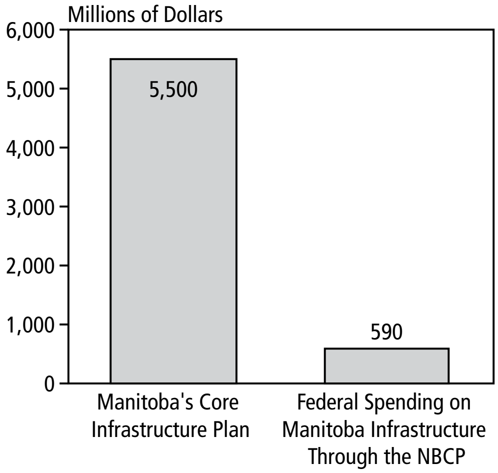
■ CONCLUSION

In 2006, the federal government committed to restoring fiscal balance and developing a stronger and more cooperative federation where governments work together on shared priorities that help Canadians realize their potential.

Manitoba appreciated the federal government's willingness to work together in response to the recent downturn in the economy. When the federal government shifted its focus to deficit reduction in 2010, it assured Canadians that the budget would not be balanced on the backs of the provinces or citizens. Despite its promises, the federal government has undertaken numerous actions that are negatively impacting provinces and territories. While these actions have helped the federal government to balance its own budget, they are shifting financial pressures onto provinces and territories at a time when demand for programs and services is growing.

Appendix: EXAMPLES OF FEDERAL ACTIONS IMPACTING PRIORITY SECTORS

Infrastructure Investments in Manitoba Over Five Years



Note: One-half of Manitoba's $1.18 billion allocation under the NBCP is assumed to be spent over five years.

Manitoba's $1.18 billion share of the NBCP includes base funding of $250 million and per capita funding of $217.1 million under the Provincial-Territorial Infrastructure Component (PTIC) and $713.7 million for municipalities under the federal Gas Tax Fund. Manitoba may receive additional federal funding under the National Infrastructure Component and P3 Canada Fund which are merit based and not allocated regionally.

Source: Manitoba Infrastructure and Transportation

Infrastructure and Transportation

In the five year period starting in 2014-15, the Government of Manitoba is committed to investing funding of more than $5.5 billion towards core infrastructure, including roads, bridges, clean water projects and flood protection. Over the next 10 years, the Government of Canada has committed to fund about $1.18 billion ($590 million over five years) worth of infrastructure development in Manitoba through the New Building Canada Plan (NBCP). When comparing infrastructure investments, Canada expenditures are only a fraction of what will be provided by the Province.

There are a number of other issues with the NBCP, including more onerous cost-sharing requirements and more restrictive program parameters. The federal government has also offloaded most of the program implementation responsibilities to the provinces. As well, program administration assistance from federal regional offices has been eliminated, resulting in the loss of three federal staff in the joint secretariat. These changes have increased the administrative burden on the province.

In 2010, the Winnipeg Partnership Agreement expired, ending almost 30 years of formal tripartite agreement/investment in Winnipeg's downtown revitalization and related social and economic development initiatives. As a result, the province announced its own five-year Winnipeg Regeneration Strategy to continue to build on the former tripartite agreement.

There have also been significant changes to the manner in which the federal government is regulating and supporting Manitoba's airport, marine and railway system. This has led to pressures on infrastructure and increased requirements on Manitoba to address shortfalls and regulatory challenges. For example, recent changes to federal grade-crossing regulations will heighten safety requirements at rail crossings, while at the same time the federal government has reduced its support for grade-crossing improvements. As a result, the province is facing both higher regulatory costs and increased pressures to backfill the reduced federal funding.

Disaster Financial Assistance

Starting in February 2015, the federal government made changes to the Disaster Financial Assistance Arrangements (DFAA), the impacts of which are of particular concern in Manitoba because of the frequency of flood events in recent years and the expectation that extreme weather-related events will increase in the future as a result of climate change.

Under the new federal rules, which raised the minimum threshold of eligibility from $1 to $3 per capita, a disaster in Manitoba has to reach $3.9 million before federal cost-sharing begins; the previous minimum threshold was $1.3 million. The maximum 90:10

cost-sharing ratio, where the federal government pays 90% of assistance costs, will not kick in until Manitoba's costs reach almost $20 million, compared to the previous threshold of $6.5 million. It is estimated that, if these changes had been in effect since 2000, the province would have had to cover an additional $54.9 million in flood assistance costs.

At their January 30, 2015 winter meeting, Canada's Premiers issued a statement expressing concern that the federal DFAA modifications "will offload additional emergency support and recovery costs onto provinces and territories. Premiers urged the federal government to reconsider its decision".

Health

With the Expiry of the 2004 Health Accord in April 2014, federal funding has ended for a number of important national programs, including the National Wait Times Initiative, and the Health Council of Canada, which monitored and reported on Health Care System Innovation. Additionally Canada Health Infoway which has been instrumental in the development of electronic medical records and Telehealth, has not received any funding since 2010 and 99% of its current funds are committed. With no new funding announced, the future of these programs and resources to support innovation remains in question.

In Manitoba, we have seen several programs where "matching" funding from Health Canada or the Public Health Agency of Canada has ended. For example, Manitoba's Chronic Disease Prevention Initiative ended in 2010 with the province picking up $600,000 per year for the last five years to maintain this important initiative.

In addition to lost funding, there have also been significant cuts to Aboriginal health care initiatives supported by the federal government. Since 2003, Health Canada has been withholding payments to Regional Health Authorities (RHAs) and Lifeflight (Manitoba Health's air ambulance program) based on a policy decision to limit funding for status (on and off reserve) First Nations clients.

Federal health related policy changes are also having impacts on provinces and territories. For example, changes to the *Canada Health Act* have resulted in health care for Royal Canadian Mounted Police officers no longer being considered a federal responsibility. As such, they have in effect created close to 1,000 new patients for the Manitoba health system. Other recently announced changes to programs such as the federal Marijuana Medical Access Program and the Interim Federal Health Program are also anticipated to have an impact in Manitoba.

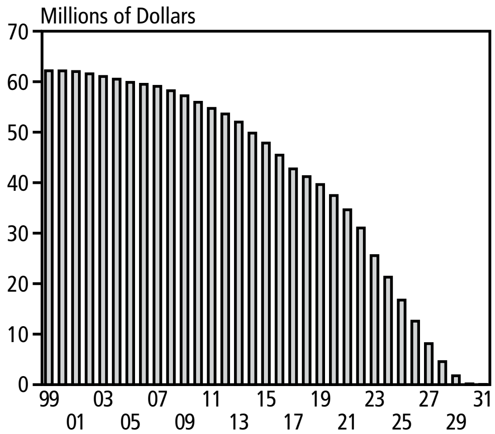
Families

In 2005, the federal government committed $5 billion nationally over five years to enhance and expand early learning and child care, in collaboration with provinces/territories, through the Early Learning and Child Care (ELCC) Bi-lateral Agreements. It is estimated that Manitoba's share of ELCC funding would have been $176 million over five years. However, the 2006 federal budget cancelled the ELCC, so the province received only first-year funding of $25.6 million. As a result of this federal action, a number of new ELCC initiatives had to be suspended or delayed. These programs were later implemented using provincial funding, but Manitoba would be much further along in its continued growth of early learning and child care had the federal government followed through on the ELCC commitment.

The province of Manitoba has been pleased to partner with the federal government and First Nation communities to provide a variety of supports and services proven to be effective in promoting positive early childhood outcomes, school readiness, mental well-being and long-term positive life outcomes. Delays in confirmation of the Education Partnership Program and the possible expiration of the Strengthening Families initiative will undermine the progress to date and negatively impact access to effective programming by First Nation families. The province will continue to partner with First Nation organizations and communities to support early childhood outcomes, as possible.

The federal government is no longer supporting services previously funded through Status of Women Canada (SWC). This includes the closure of the Manitoba regional office and the narrowing of the mandate of SWC, resulting in over 30 women's organizations that once received funding through SWC's Women's Program having their funding reduced or eliminated completely. Additionally, the elimination of the Court Challenges Program, which provided an essential source of financial assistance for important court challenges based on equality of protected groups, including women, greatly diminished the capacity of Canadians to advance the gender equality guaranteed under the constitution.

Federal Funding - Social Housing Agreement



Source: Manitoba Housing and Renewal Corporation (Social Housing Agreement, Schedule E)

Social Housing

The federal government's support for social housing in Manitoba has been eroding. Since 1999, federal subsidy levels under the Social Housing Agreement (SHA) have declined. By 2022, the annual transfer to Manitoba under the SHA will be 50% of what it was in 1999. In 2006, the federal government provided nearly $60 million under the SHA. However, by 2032 the federal government will have discontinued all SHA funding. This declining cash flow from the federal government poses a major financial challenge in maintaining social and affordable housing programming in Manitoba.

Justice

Over the past decade, Manitoba has had to fund 100% of the increase in the costs of criminal legal aid and youth justice services as the federal government has not increased funding levels since entering into these cost-sharing agreements with the province. For example, Manitoba currently receives $4.7 million in funding from the federal government for legal aid, representing only a small fraction of the total legal aid cost in Manitoba. Manitoba spent $26.3 million on legal aid in 2014/15.

In addition, funding for youth criminal justice services had been held flat since 2006, and was actually reduced by $1.3 million in 2013. This means the federal share of expenditures on youth criminal justice services in Manitoba have fallen from 20% to 9%. The program helps pay for probation services for youth, prevention programs for youth at risk of committing a crime and rehab programs to keep them from re-offending when they are released from jail.

Canada has also reduced its commitment to a number of policing initiatives, including terminating the Band Constable Program effective March 31, 2015, refusing to increase its funding for the four-year agreements with Manitoba (2014/15 to 2017/18) for the First Nation Policing Program, and eliminating the federal Police Officers Recruitment Fund.

Immigration

In 2012, the federal government informed Manitoba of its unilateral decision to cancel the Settlement Annex. Citizenship and Immigration Canada (CIC) assumed responsibility for the direct administration of settlement service funding in 2013. The new federal eligibility criteria for allocating settlement funding are more restrictive than was the case under devolved provincial administration. As a result, some programs have been cut or have had their funding reduced and a number of clients can no longer access free services. The lack of formal and effective co-ordination mechanisms between CIC and the province has exacerbated a growing gap in services.

Since 2006/07, the federal government has also cut or reduced other immigration programs, such as Enhanced Language Training, Welcoming Communities Initiative (anti-racism), Immigration Portal Initiative, Destination Canada and the federal Immigrant Investor Program.

Economic Development

The Canada-Manitoba Economic Partnership Agreement (EPA) ended September 30, 2013. The absence of a joint-funding agreement limits the opportunity for organizations to leverage non-government funding. Manitoba has provided two-year Economic Development Initiative (EDI) funding to the majority of those organizations previously supported through EPA. As well, the limited flexibility and prescribed funding approach now utilized by the federal government is ultimately impacting the type and amount of funding received by these organizations. Funding shortfalls related to National Research Council supported programs and infrastructure have also led to a loss of capacity where Manitoba has not been able to backfill.

As of March 31, 2013, funding for the national Sector Council Program has been discontinued. Despite projected program and staffing reductions, Manitoba Sector Councils have done their best to manage these cuts without negatively impacting their organizations.

Environment and Agriculture

In an effort to reduce expenditures, the federal government made a decision to close the internationally renowned Experimental Lakes research facility. Recognizing the importance of this initiative, Manitoba has partnered with Ontario to ensure this important work continues. The province has entered into a new $6 million six-year arrangement with the International Institute for Sustainable Development. Of this, $900,000 is intended to support the Experimental Lakes Area initiative.

Several services previously administered by the Canada Food Inspection Agency have now been devolved or returned to the province, including the provincial Meat Inspection and Disease Management programs which cost Manitoba Agriculture, Food and Rural Development an estimated $3 million in the years 2012/2013, 2013/2014 and 2014/2015. The responsibility for the Rabies Health Program is expected to cost Manitoba close to $1 million annually. Also, the federal government has withdrawn funding from important research areas that directly impact economic activity including wheat quality testing, beef and crop diversification.

Another example is the federal government’s decision to divest itself from the Community Pasture Program. In response, Manitoba has committed $1.2 million over three years for a pilot project with a new not-for-profit entity in an effort to ensure the continued availability of community pastures. The new program will be much reduced compared to the original program and will likely require some on-going support from the province.