
Medicare's unfunded liabilities

*Milagros Palacios &
Nadeem Esmail*

WHILE some still cling to the false notion that Canada's health care system is among the best in the world, their beliefs are not supported by the evidence, which clearly shows that the system is in dire straits (see, for example, Esmail and Walker, 2008; Esmail and Walker with Hazel, 2008). Canadians collectively spend more on health care than their counterparts in almost all other industrialized OECD countries, but receive relatively poor access to health services in return (Esmail and Walker, 2008).

Worse still, the portion of government revenue currently used to pay for Medicare will not be sufficient to fund future medical expenses. In other words, governments have promised to provide health care that the current tax rates leave unfunded. Unless immediate action is taken to reduce Medicare's unfunded liabilities, young Canadians will be hit with a significantly larger tax bill in the future.

Medicare's unfunded liabilities

AN "unfunded liability" is the shortfall between the future stream of funding for a program and its future obligations (expenditures). Put simply, it is the difference between what we might expect to spend on health care in the future and what we might expect to have available to actually pay for health care.

Medicare is funded through general government tax revenues.¹ There are

no specific funding sources set aside to pay for Medicare benefits²; all services are funded on a "pay-as-you-go" basis whereby current government revenues and borrowing fund current health expenditures.

At its inception, Medicare was based on the assumption that the demographics prevailing in the 1960s would persist. It was considered favourable social and economic policy to transfer a small amount of money from a large group of younger workers to benefit a small group of older and relatively less well-off retirees (Palacios et al., 2008).

Unfortunately, demographic assumptions have proven false. In 1956, the proportion of the Canadian population that was under 20 years of age was 39.4%, while the proportion of those over 65 was 7.7%. By 2007, the percentage of the population under 20 years old had decreased to 23.7%, while the ratio of those over 65 had increased to 13.4% (Statistics Canada, 2008). Statistics Canada predicts that by 2040, those under 20 will account for 17.2% of the total population, while those 65 and over will account for 26.5% (Statistics Canada, 2005).³

In 2007/2008, Medicare consumed 19.5% of total federal, provincial, and local government revenue (Statistics Canada, Public Institutions Division, 2008). Given that seniors (persons over 65 years old) account for approximately 44% of all health spending, and that the percentage of seniors will increase dramatically in the coming years, the portion of revenue currently used to fund

Medicare will not be sufficient to pay for medical expenses in the future.

This change in Canada's demographic makeup will continue to increase the amount of revenue needed to fund Medicare expenditures. We estimate that the difference between the stream of promised benefits and the expected future stream of revenues—the unfunded liability of Medicare—was \$364 billion in 2004, the latest year for which the estimate is available (Palacios et al., 2008).⁴ Medicare's unfunded liability grew by 20.7% between 2000 and 2004, from \$301.5 billion to \$364.0 billion (table 1).

Conclusion

CANADA'S Medicare system is failing Canadians today—by delivering relatively poor access to health care services, despite having a world class price tag—and tomorrow through a substantial unfunded liability. Without fundamental reform to Canada's health care system, young Canadians will be digging much deeper to pay their future tax bills.

Notes

¹ This is also true in provinces that levy health care premiums (British Columbia, Ontario, and formerly Alberta), as those premiums are paid into general revenues and health expenditures are paid from general revenues.

² Nor is there a stock of assets that have been set aside to pay for future Medicare obligations.

³ These estimates are based on projections by Statistics Canada (2005) assuming a medium growth scenario.

⁴ In order to calculate the unfunded liability of Medicare, the discounted stream of future benefits and the discounted stream of future contributions were calculated using a model developed by the Fraser Institute. A description of the model and its assumptions can be found in Palacios et al. (2008).

Table 1: The unfunded liability of Canada's health care system

Fiscal year	Medicare's unfunded liability (billions of \$)
2000	\$301.5
2001	\$323.0
2002	\$331.1
2003	\$347.0
2004	\$364.0
Change from 2000 to 2004 (%)	20.7%

Source: Palacios et al., 2008.

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