Supplementary Estimates (C) 2014-15

Ottawa, Canada
February 26, 2015
www.pbo-dpb.gc.ca

The mandate of the Parliamentary Budget Officer (PBO) is to provide independent analysis to Parliament on the state of the nation's finances, the government's estimates and trends in the Canadian economy; and upon request from a committee or parliamentarian, to estimate the financial cost of any proposal for matters over which Parliament has jurisdiction.

This note presents detailed analysis of the federal government's fifth and final appropriation bill for the 2014-15 fiscal year.

Prepared by: Negash Haile and Jason Jacques

* Please contact Mostafa Askari (mostafa.askari@parl.gc.ca) for further information.

The Bottom Line

- The Government of Canada (Government) is asking parliamentarians for $1.8 billion in new money to implement the spending plan outlined in Budget 2014. This increase is partially offset by $1.3 billion in downward revisions to spending estimates for other statutory programs, resulting in a net increase of $0.5 billion.

- The funding requested in these Supplementary Estimates is consistent with the composition of previous years, with proposed year-end increases in Direct Program Spending offset by decreases in estimated spending requirements on major transfers and debt interest costs.

- Beyond the proposed new budgetary spending, these Supplementary Estimates also propose new “non-budgetary” spending of $246 million, primarily in the form of loans to third-parties. The magnitude of “non-budgetary” expenditures grew prodigiously over the past five years due, primarily, to the federal response to the 2008 global financial crisis.

- “Government Affairs” would receive the largest increase in new money, linked to a $646 million increase in the Treasury Board Secretariat’s *Government-Wide Funds and Public Service Employer Payments* program, which is primarily responsible for administering the overall compensation and benefit regime for the Government of Canada.

1 The Government Needs the Estimates to Implement its Budget

Each year, Parliament endorses the Government’s fiscal and economic strategy outlined in the Budget. The Government then needs to obtain Parliament’s approval of the money required to implement its Budget. This legal consent is provided in one of two ways:

a) **Ongoing statutory authority**, through standing legislation that allows federal departments and agencies to expend funds for specific purposes, when needed. Examples of this are the cost of Old Age Security benefits and Public Debt Interest expenses. In 2014-15, over 60% of planned budgetary spending is authorized through these standing mechanisms.

b) **Time-limited, voted, appropriations**, which Parliament approves each year for the separate operating, capital and transfer payment budgets of departments and agencies. With certain exceptions (for example, Parks Canada, the Canada Border Services Agency and the Canada Revenue Agency), the legal authority to spend this money expires at the end of the fiscal year (that is, March 31). In 2014-15, a little less than 40% of the Government’s planned budgetary spending will be authorized through this mechanism.[1]

The Government typically presents five separate appropriation bills to Parliament each year to obtain annual spending authority. The first two are the largest and correspond to the Government’s Main Estimates, which seek authority for roughly 95% of the total spending

[1] Any annual “voted” appropriations that remain unspent by the end of the fiscal year will offset the deficit (or augment the surplus) and automatically reduce public debt.

in a given year. The other three appropriation bills correspond to the Supplementary Estimates, through which the Government seeks Parliament's approval to spend money on initiatives that were "either not sufficiently developed…at the time of the Main Estimates…or…have been further refined..".[2]

Non-Budgetary Transactions

Beyond the actual spending proposed in the Budget, the Government's Estimates also present details regarding "non-budgetary" transactions. These expenditures are comprised of loans and investments that create an offsetting asset on the Government's financial statements. Examples include loans provided to First Nations and advances to international organizations, such as the International Monetary Fund.

Unlike budgetary authorities, non-budgetary spending authorities generally do not expire at the end of a given fiscal year. Rather, Parliament provides its consent for the transaction itself. The timing and amount of the repayment typically extends beyond a single fiscal year and is not necessarily specified.

The magnitude of these non-budgetary transactions grew prodigiously over the past five years, as part of the Government's response to the 2008 global financial crisis (Box 1-1).

Box 1-1

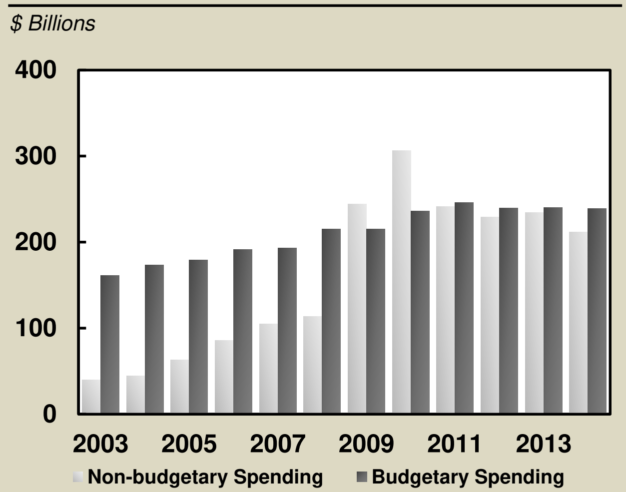
Non-Budgetary Transactions

According to the Public Accounts of Canada, the amount of non-budgetary spending authorities has grown substantially over the past decade, from $39.7 billion in 2002-03 to $211.5 billion in 2013-14.

Non-budgetary transactions were historically much smaller than annual budgetary spending (2002-03 to 2007-08), albeit growing at a faster rate. This changed in 2008-09 as non-budgetary expenditures more than doubled to $244.1 billion, when the Government expanded its repayable financial support and directly purchased other financial assets in response to the 2008 global financial crisis.

Since peaking at over $306 billion in 2009-10, the size of the loans and other "non-budgetary" authorities has declined. The 2014-15 Estimates to date (Main and Supplementary) suggest they will decrease by a further $9.7 billion this fiscal year.

A Burgeoning Balance Sheet



Sources: Parliamentary Budget Officer; Government of Canada.

[2] Since the renewal of the Government's Expenditure Management System in 2007, Parliament has been presented with a Supplementary Estimates for each of the three parliamentary Supply periods ending June 23, December 10, and March 26. Supplementary Estimates (C) corresponds to the third and final Supply period. Supplementary Estimates (C) 2014-15. Accessed February 2015.

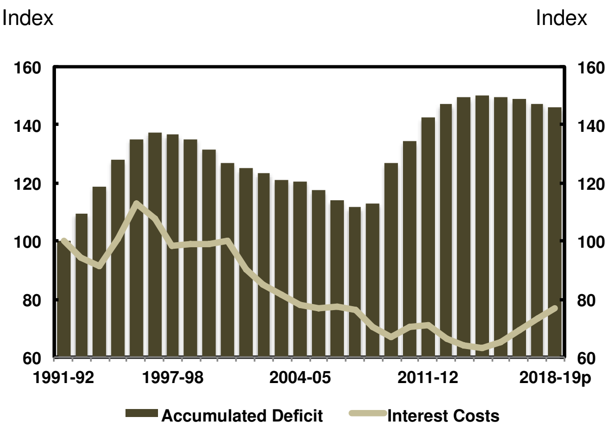
2 Lower Debt Interest Expenses Shrink Supplementary Estimates (C)

The Government's medium-term fiscal strategy to temper spending growth and return to a budgetary surplus relies on reducing Direct Program Expenses (DPE), which are the cost of Government operations and grant and contribution programs.

Beyond this intentional fiscal strategy, the Government has also benefitted from a lower-than-anticipated global interest rate environment, which has resulted in debt-interest expenses decreasing over the past five years even as the size of the federal debt has grown to a record high (Figure 2-1). This fiscal dividend has been significant: Budget 2010 projected that Public Debt Interest expenses would reach $40.6 billion in 2014-15, whereas the 2014 Update of Economic and Fiscal Projections projected that this figure would be $12.9 billion lower.[3]

Figure 2-1

Falling Global Interest Rates Provide Additional Fiscal Room



Sources: Fiscal Reference Tables; Economic and Fiscal Update 2014.

Note: Figures from 2014-15 onward are projections.

Reflecting the historically low interest rate environment, these Supplementary Estimates propose that Parliament vote to approve $1.8 billion in new spending, which is partially offset by $1.3 billion in downward revisions to estimated statutory expenses – including $1.1 billion in reduced interest costs on the national debt (Figure 2-2).[4]

Figure 2-2

Supplementary Estimates (C)

Billions

	Budgetary	Non-Budgetary
Voted	$1.783	-
Statutory	*-$1.288*	*$0.246*
Total	**$0.495**	**$0.246**

Source: Supplementary Estimates (C) 2014-15.

Overall, the adjustment would bring total budgetary authorities for 2014-15 to approximately $242.1 billion, up 1.3% over the total budgetary authorities approved last year.[5]

Notwithstanding the $246 million upward revision to non-budgetary authorities presented in Supplementary Estimates C, the Government estimates that overall non-budgetary authorities for 2014-15 are on track to decrease $9.7 billion.

Roughly 60% of the new spending (that is, budgetary authorities) requested would go toward increased operating spending by departments and agencies (Figure 2-3). Slightly more than 30% would be transferred by the Government to external parties, such as private organizations, other levels of government, or individuals. The balance would be invested in capital assets owned by the Government.

[3] The lower debt interest costs also reflect, in part, lower than anticipated deficits over the five-year period as well. Budget 2010; 2014 Update of Economic and Fiscal Projections. Accessed February 2015.

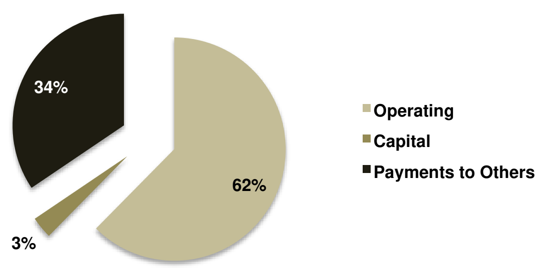
[4] As noted earlier, Parliament provides pre-existing legislative authority to spend under other legislation for "statutory" spending, hence parliamentarians are not asked to approve the revisions to these estimates.

[5] Based on budgetary authorities presented in the Main and Supplementary Estimates in 2013-14, less Employment Insurance spending, which is no longer presented in the Government's Spending Plan.

Figure 2-3

How the Government Plans to Spend the Supplementary Estimates (C) Money

% of total Budgetary Authorities



Sources: Parliamentary Budget Officer; Government of Canada.

Note: Figures presented are exclude the downward revision to estimates of debt interest expenses.

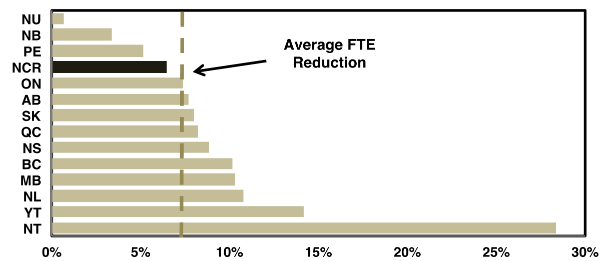
Over three-quarters of the new operating spending would be directed toward personnel expenses ($754 million), which are estimated to rise to $39.5 billion in 2014-15, marginally higher than the previous year (+0.3%).

One-time, non-recurring, factors explain the increase in total salaries and benefits provided to federal employees (discussed in greater detail in the subsequent section). As noted in previous PBO reports, total personnel costs have fallen from their 2012-13 peak owing to the elimination of 20,954 positions in the federal public service since March 31, 2012.

As noted in Figure 2-4, staffing cuts over the past two years have disproportionately affected employees outside of the National Capital Region. While the overall employment reduction across the federal public service was 7.5%, the commensurate figure for the National Capital Region (NCR) was 6.5%. Overall, almost two-thirds of employment reductions have fallen outside of the NCR, raising its share of total federal employment to over 42%.

Figure 2-4

Axe Falls Harder Outside of Ottawa



Sources: Parliamentary Budget Officer; Government of Canada.

3 Priorities in “Government Affairs” to Receive Most Proposed Funding

Most of the new spending would be concentrated on the “Government Affairs” ($782 million), followed closely by “International Affairs” ($441 million) and “Social Affairs” ($136 million). Primarily owing to the downward revision to estimated Public Debt Interest costs, spending on “Economic Affairs” would fall by $864 million. (Figure 3-1; Box 3-2).[6]

Much of the increase in Government Affairs is attributable to growth in the Treasury Board Secretariat’s *Government-Wide Funds and Public Service Employer Payments* program, which would rise $646 million (+8.9%). According to the department’s Report on Plans and Priorities for 2014-15, the objective of this program is to “meet certain responsibilities of the Treasury Board as the employer of the core public administration, including employer obligations under the public service pension and benefits plans”.[7]

[6] Treasury Board Secretariat’s Whole of Government Framework. Accessed February 2015.

[7] Treasury Board Secretariat 2014-15 Report on Plans and Priorities. Accessed February 2015.

Figure 3-1

Largest Share of New Funding for Government Affairs and the Employee Compensation Regime

Thematic Spending Area	Supplementary Estimates C (*Millions*)	Share of Net New Money in Supplementary Estimates C	Revised Total Estimates (*Millions*)	% Change
Economic Affairs	**-$ 864**	**-175%**	**$ 161,318**	**-1%**
Strong Economic Growth	-$ 876	-177%	$ 102,733	-1%
Income Security and Employment for Canadians	-$ 367	-74%	$ 48,870	-1%
An Innovative and Knowledge-based Economy	$ 349	71%	$ 6,523	5%
A Clean and Healthy Environment	$ 12	2%	$ 2,649	0%
A Fair and Secure Marketplace	$ 17	4%	$ 542	3%
Social Affairs	**$ 136**	**28%**	**$ 48,318**	**0%**
A Diverse Society that Promotes Linguistic Duality and Social Inclusion	$ 24	5%	$ 11,215	0%
A Safe and Secure Canada	$ 27	6%	$ 28,426	0%
Healthy Canadians	$ 78	16%	$ 6,737	1%
A Vibrant Canadian Culture and Heritage	$ 7	1%	$ 1,940	0%
International Affairs	**$ 441**	**89%**	**$ 7,370**	**6%**
Global Poverty Reduction Through International Sustainable Development	$ 115	23%	$ 3,334	3%
A Safe and Secure World Through International Engagement	$ 320	65%	$ 3,776	8%
A Prosperous Canada Through Global Commerce	$ 6	1%	$ 260	2%
Government Affairs	**$ 782**	**158%**	**$ 24,233**	**3%**
Well-managed and efficient government operations	$ 755	153%	$ 22,205	3%
A Transparent, Accountable and Responsive Federal Government	$ 11	2%	$ 1,207	1%
Strong and Independent Democratic Institutions	$ 16	3%	$ 820	2%

Note: Spending classifications exclude the Employment Insurance Account, which the Government excludes from the "Whole of Government Framework". Finance Canada's *Transfer and Taxation Payment* program is assumed to be classified under **Economic Affairs**: Strong Economic Growth. Total amounts and total percentage changes do not reflect transfers from Treasury Board Central Votes or inter-year transfers made to the budgetary authorities for the three federal organizations with multi-year appropriations, as this data is not disclosed by the Government on a program activity basis.

Box 3-2

Viewing Government Spending Through a Policy Lens

The Government's Whole of Government framework classifies all federal spending in four thematic areas:

- Economic Affairs
- Social Affairs
- International Affairs
- Government Affairs

Each of the four areas of spending are then linked to 15 discrete "outcome areas", which identify the primary objective of the spending. For instance, "Social Affairs" has four outcome segments: *Healthy Canadians*; *A Safe and Secure Canada*; *A Diverse Society that Promotes Linguistic Duality and Social Inclusion;* and, *A Vibrant Canadian Culture and Heritage*.[8]

Analyzing departments' and agencies' spending by policy category provides greater clarity regarding the Government's priorities and what it expects to achieve.

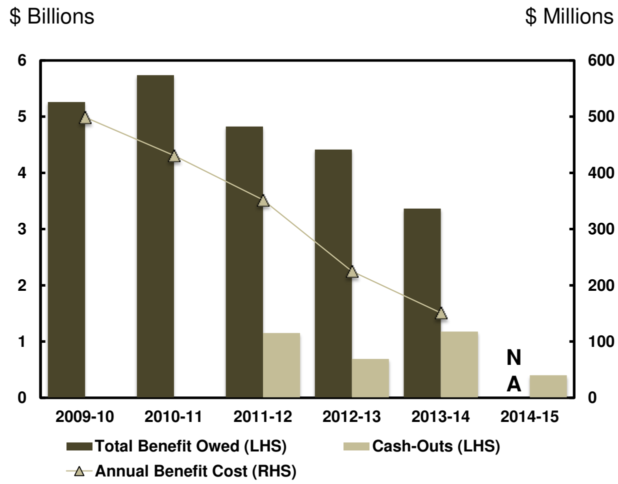
The proposed overall funding increase is linked to three factors: to reimburse departments and agencies for the "cash-out" of employee severance pay benefits ($400 million); higher than anticipated demand for veterans' long-term disability benefits ($196 million); and, benefit enhancements for the Public Service Health Care Plan ($50 million).

Since 2010, the Government has made an ongoing effort to phase out a voluntary departure benefit for federal employees, which provided departing federal employees one week of salary for each year of service.

In 2009-10, the Public Accounts of Canada indicate that the annual cost of this benefit was close to $500 million (Figure 3-3). Since then, the elimination of this benefit provision in collective agreements reduced the annual expense to $151 million in 2013-14.

Figure 3-3

Eliminating Employee Benefits Generates Ongoing Fiscal Savings



Sources: Parliamentary Budget Officer, Government of Canada

New money for "International Affairs" is the second largest area of new spending in Supplementary Estimates (C). Over two-thirds of the increase is attributable to the *Safe and Secure World Through International Engagement* outcome ($320 million, +8%).

The majority of this funding increase is targetted toward the Department of Foreign Affairs, Trade and Development's *Diplomacy and Advocacy* program ($152 million, +16%), in particular the Stabilization and Reconstruction Task Force (START). As noted by the department, START has four key objectives:

- "Provide leadership and … coordinate(d) responses to international crises;
- Deliver…programming in support of conflict management and peace-building, peacekeeping and peace operations;
- Serve as a centre of policy excellence on fragile states and peace operations; and,
- Serve as the Government of Canada's ability to respond to crisis situations."[9]

[8] Treasury Board Secretariat's Whole of Government Framework. Accessed February 2015.

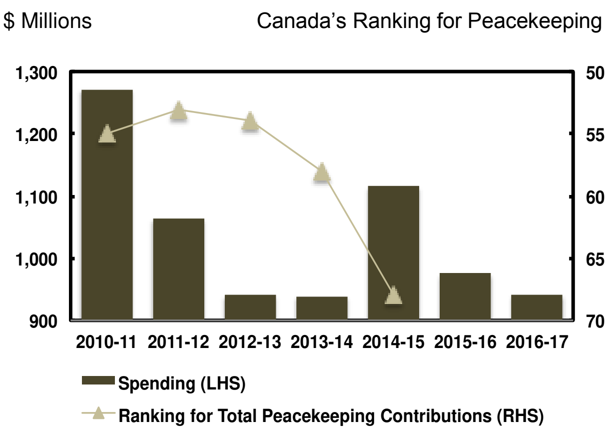
[9] Department of Foreign Affairs, Trade and Development ("About START"). Accessed February 2015.

Notwithstanding the proposed increase in these Supplementary Estimates, over the past few years funding for the *Diplomacy and Advocacy* program has decreased, falling from a peak of $1.27 billion in 2010-11 to $1.11 billion in 2014-15 (Figure 3-4). The department's Report on Plans and Priorities projects that spending on this program will fall further over the next two years, to $941 million in 2016-17 ($174 million lower, or -16%).[10]

Beyond the decrease in resources, this program also mirrors the shifting priorities of the Government in its funding of international operations. The United Nations' ranking of peacekeeper contributions could reflect these changes, as Canada's international ranking for the number of personnel committed to peacekeeping operations has fallen from 55th in 2010 to 68th in 2014.[11]

Figure 3-4

Decreased Funding and Shifting Priorities for Canadian Diplomacy



Sources: Parliamentary Budget Officer, Government of Canada, United Nations.
Note: Figures from 2010-11 to 2013-14 are actual expenditures; 2014-15 cumulative Estimates; and 2015-16 onward from the Report on Plans and Priorities.

The last policy area with a material change is "Economic Affairs" ($864 million lower, or -1%). The aforementioned decrease in estimates for Public Debt Interest costs, accounted for in the Strong Economic Growth theme, overshadows other substantial shifts in the *Income Security and Employment for Canadians* theme ($367 million lower, or -1%) and *An Innovative and Knowledge-Based Economy* theme ($349 million higher, or +5%).

Both changes are linked to programs administered by Employment and Social Development Canada (ESDC).

The decrease in the former is principally linked to downward revisions to the cost estimates for elderly benefits (that is, Old Age Security, the Guaranteed Income Supplement and Spousal Allowance), which are provided through ESDC's *Income Security* program. The department has reduced its estimates for elderly benefits payments by $425 million to $43.8 billion in 2014-15 (-1%).[12]

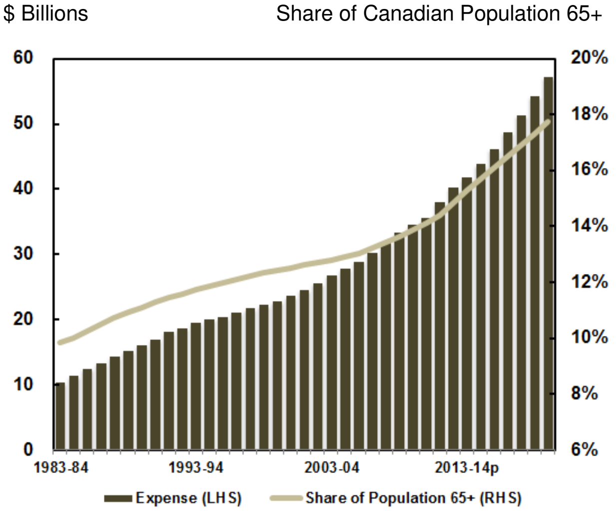
Notwithstanding the downward revision, elderly benefits will remain the single largest expense in the federal budget and are projected to rise to over $50 billion per year by 2017-18 (Figure 3-5). This growth is driven by an ageing Canadian population and Consumer Price Inflation, to which the benefits are indexed.

[10] Department of Foreign Affairs, Trade and Development's 2014-15 Report on Plans and Priorities. Accessed February 2015.
[11] United Nations Peacekeeping Statistics. Accessed February 2015.

[12] The decrease impacts the forecasted expenditures and not the actual benefits paid.

Figure 3-5

Ageing Demographics Driving Projected Increases in Federal Elderly Benefits



Sources: Parliamentary Budget Officer, Government of Canada.

The increase in the latter is primarily attributable to ESDC's *Learning* program (up $351 million, or 16%). This program helps Canadians participate in post-secondary education and adapt to changing labour market conditions through financial support and information resources.[13]

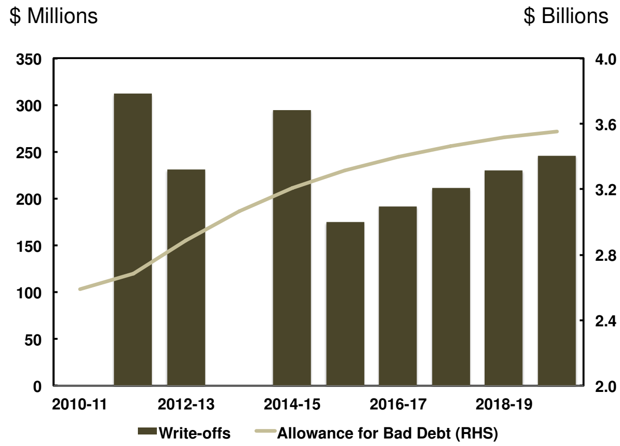
Most of the new spending relates to funding required to write-off Canada Student Loan debts ($295 million). This additional amount would bring cumulative requests for write-offs since 2011-12 to $838 million.

According to the Office of the Superintendent of Financial Institutions' (OSFI's) Actuarial Report on the Canada Student Loans Program, the allowance for bad debt (that is, loans issued that students are unable to repay as expected) is projected to rise to over $3.5 billion by 2019-20 (Figure 3-6).[14]

Commensurate with this, student loan write-offs are also projected to grow, rising to close to $250 million per year by 2019-20.

Figure 3-6

Student Debt Allowances and Write-offs Projected to Rise



Sources: Parliamentary Budget Officer, Government of Canada.

[13] Employment and Social Development Canada's 2014-15 Report on Plans and Priorities. Accessed February 2015.

[14] Actuarial Report on the Canada Students Loan Program 2011. Accessed February 2015.