OFFICE OF
THE PARLIAMENTARY BUDGET OFFICER

BUREAU DU
DIRECTEUR PARLEMENTAIRE DU BUDGET

CANADA

Main Estimates 2014-15

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Key Points of this Note:

- The Government's *Expenditure Plan and Main Estimates* for 2014-15 (Expenditure Plan) outlines $235.3 billion in planned spending for the coming fiscal year (April 2014 to March 2015).
    - This is $3.8 billion lower than the total budgetary authorities sought in the previous fiscal year (1.6 per cent), reflecting the ongoing fiscal strategy to return to a balanced budget.
- Overall, $5.9 billion in increases in major transfers to persons and other levels of government are more than offset by a $9.7 billion decline in authorities for direct program expenditures (DPE).
    - DPE cuts reflect an additional $3.8 billion of spending restraint, focused on targeted reductions to personnel and professional services contracts.
    - Spending reductions are particularly pronounced in Internal Services (*i.e.* the "back office"), which are estimated to fall almost 11 per cent to $8.4 billion.
- The Government no longer includes Employment Insurance spending in its Expenditure Plan. In addition, a growing proportion – almost two thirds - of federal spending is "statutory" in nature and does not require annual approval by Parliament.
    - Parliament lacks a well-articulated review process for statutory expenditures. As such, an increasing proportion of federal spending receives cursory oversight.

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1. Purpose

The Parliamentary Budget Officer's (PBO) legislative mandate includes research and analysis regarding the Government of Canada's (Government) Estimates.[1] To implement this, the PBO reviews the Estimates and highlights proposed adjustments that warrant scrutiny, including:

i. Proposed changes to programs that are material to adjustments in the federal budget balance; and,

ii. Proposed changes to programs that represent significant growth compared to the status quo.

While Parliament will continue to only appropriate on inputs (*e.g.* operating or capital expenditures), parliamentarians have been clear that a program lens provides greater insight. As such, the PBO's Estimates analysis focuses on authorities delineated by program.

2. Main Estimates 2014-15

The Government's *Expenditure Plan and Main Estimates* for 2014-15 (Expenditure Plan) outlines $235.3 billion in planned spending for the coming fiscal year (April 2014 to March 2015). This is $3.8 billion lower than the total authorities sought in the previous fiscal year (1.6 per cent).[2]

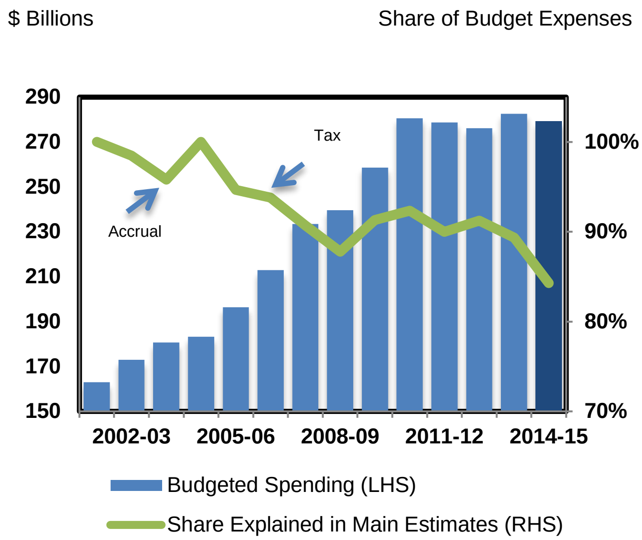
Beyond the decrease in the level of planned spending, this Expenditure Plan no longer presents planned spending on Employment Insurance (EI). While the Government correctly notes that from a legal and accounting perspective "The Employment Insurance Operating Account is a separate account in the accounts of Canada", the choice to exclude $17.7 billion in projected spending from its Expenditure Plan makes it more challenging to reconcile these figures with the projection presented last month in Budget 2014.[3]

Some parliamentarians have historically noted that the lack of concordance between the Main Estimates and Budget hinders their ability to "connect the dots" and provide effective scrutiny of proposed spending.[4]

As presented in Figure 2-1, the planned level of spending in the Expenditure Plan historically reflected most of the comparable figure presented in the Budget.

Figure 2-1

Less Spending Explained in Main Estimates



Sources: *Main Estimates* and *Budget Plan*

Note: Budget Expenses are taken from each annual Budget Plan's next year expense forecast.

The Government's shift to present the Budget on a different basis of accounting from the Expenditure Plan (*i.e.* accrual versus cash)

[1] http://laws-lois.justice.gc.ca/eng/acts/P-1/FullText.html?term=79.2. Accessed March 2014.
[2] http://www.tbs-sct.gc.ca/ems-sgd/me-bpd/20142015/me-bpd-eng.pdf. Accessed March 2014.

[3] http://www.budget.gc.ca/2014/docs/plan/ch4-2-eng.html. Accessed March 2014.
[4] The Seventh Report of the House of Commons Standing Committee on Government Operations; 41st Parliament, First Session. http://www.parl.gc.ca/HousePublications/Publication.aspx?DocId=5690996&File=135. Accessed March 2014.

opened a gap in 2003-04. A subsequent decision to further adjust Budget in 2006-07 and present the Canada Child Tax Benefit as an expense (rather than netting it from personal income tax revenues) exacerbated this gap.

The decision taken this year to no longer reflect projected EI spending in the Expenditure Plan will result in less than 85 per cent of the projected spending in the Budget being reflected in these Estimates.

While the Government historically provided a reconciliation table between the Expenditure Plan and Budget in the Estimates document, this has not been done in recent years. As a consequence, parliamentarians no longer have a tool to harmonize these two sources of planned spending data.

Concurrent with this trend to reflect less planned spending in the Expenditure Plan, there has also been a shift in the parliamentary procedure through which funding is approved.

As presented in Figure 2-2, the share of planned spending authorized by standing legislation (*i.e.* “statutory” authorities, such as the Canada Health Transfer) have increased and those requiring annual authorization (*i.e.* “voted” authorities, such as the operating budgets of departments and agencies) have therefore fallen.

Procedurally, this results in less money being scrutinized by existing parliamentary review mechanisms. While the *Financial Administration Act* stipulates that every department and agency must complete a five-year review of their grants and contributions programs, this excludes programs with independent “statutory” payment authorities. [5] As well, Parliament lacks a corresponding standing review mechanism to consider the five-year reviews prepared by the Government.

[5] http://laws-lois.justice.gc.ca/eng/acts/F-11/page-25.html#docContAccessed March 2014.

Figure 2-2

Less Spending Annually Scutinized by Parliament

$ Billions; % of total authorities

	Statutory		Voted	
	$	***%***	**$**	***%***
2012-13	**139.86**	*61*	**87.71**	*39*
2013-14	**145.16**	*61*	**93.94**	*39*
2014-15	**149.05**	*63*	**86.28**	*37*

Source: *Main Estimates 2014-15*.

Notes: Figures for 2012-13 represent actual expenditures; figures for 2013-14 are cumulative authorities; figures for 2014-15 are Main Estimates.

Evolution of the Government’s Expenditure Plan

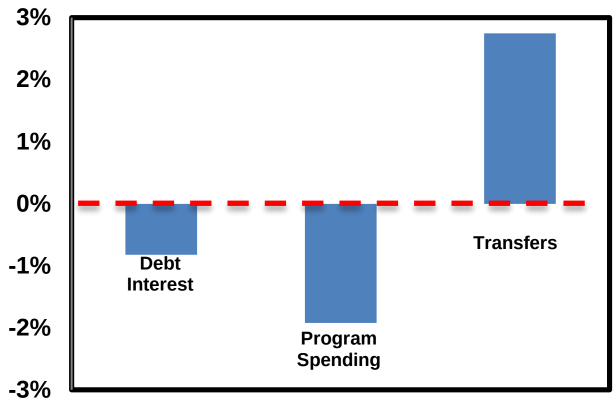
As noted in previous PBO reports, aside from the temporary stimulus initiatives, the underlying composition of ongoing spending has maintained a steady trend over the past five years. The share of total spending earmarked for debt interest costs and program spending has fallen, offset by increases in transfer payments (Figure 2-3).

The 2014-15 Expenditure Plan continues this trend. Compared to total spending authorities in the previous year, transfers to other levels of government and major transfers to individuals (*e.g.* Old Age Security Benefits) are estimated to rise by $4.6 billion and $1.3 billion, respectively. Offsetting this is $9.7 billion in decreases to Direct Program Expenditures (DPE), resulting in a net decrease in planned spending of $3.8 billion (Figure 2-4).

Figure 2-3

Five-Year Realignment of Spending Priorities

Net Per cent Change in Shares from 2009-10 to 2014-15



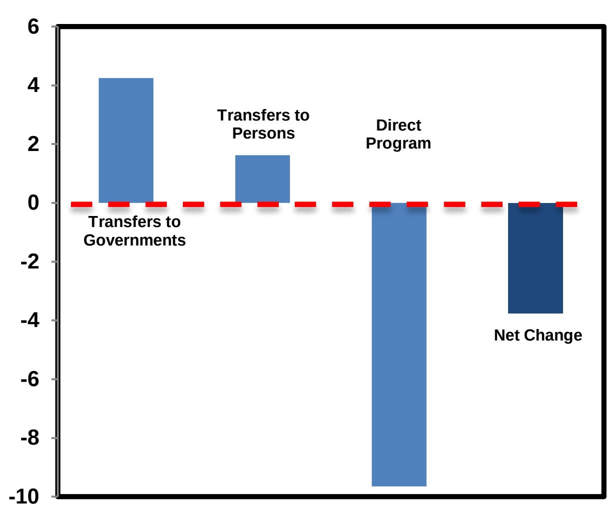
Sources: Public Accounts of Canada 2009-10 to 2012-13, *Main Estimates* 2013-14.

Notes: Figures for 2012-13 represent actual expenditures; figures for 2013-14 are cumulative authorities; figures for 2014-15 are Main Estimates.

Figure 2-4

Year-over-Year Changes in Planned Spending

$ Billions



Sources: *Main Estimates* 2013-14.
Notes: Comparison between 2013-14 cumulative Estimates to date and 2014-15 Main Estimates.

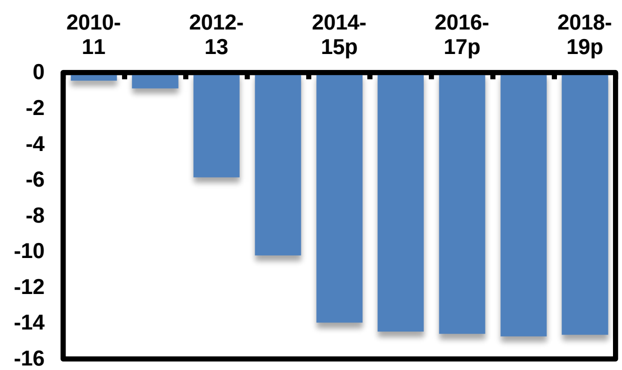
The planned reduction in DPE results from the Government's successive restraint initiatives, which targeted this area of spending comprised of the government operations, as well as grants and contributions programs.

As depicted in Figure 2-5, the cumulative effect of spending restraint since 2009-10 will reduce planned DPE by $10.2 billion in the current year (2013-14), rising to almost $14.0 billion in the coming fiscal year (*i.e.* a further $3.8 billion cut).

Figure 2-5

Cumulative Impact of Spending Restraint

$ Billions



Source: Budget 2014.
Note: Data from 2013-14 onward are projections.

The areas of DPE projected to have some of the largest reductions in 2014-15 compared to the previous year are personnel, professional services, particularly those related to "overhead" or back-office costs in Government. This is consistent with the commitment in the Speech from the Throne.[6]

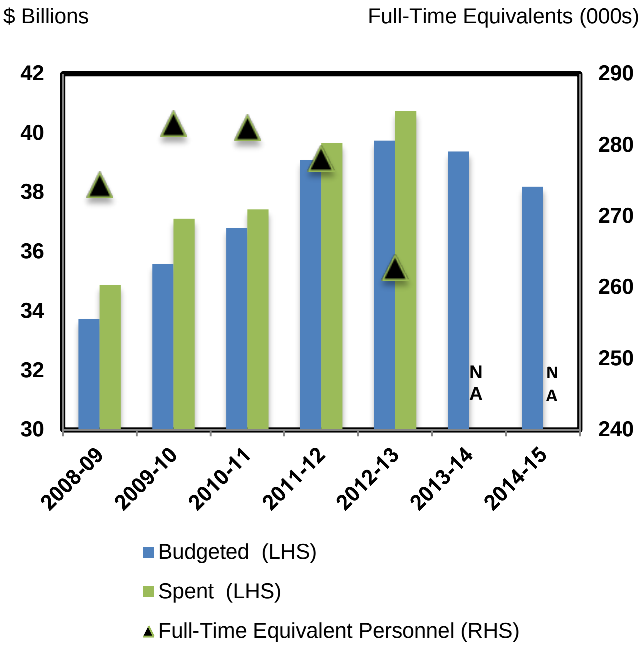
[6] http://speech.gc.ca/sites/sft/files/sft-en_2013_c.pdf. Accessed March 2014.

Personnel Costs

Personnel costs reflect the annual expense for public service salaries and benefits.[7] In 2014-15, spending on *Personnel* is estimated to decline by $1.2 billion to $38.2 billion (0.9 per cent; Figure 2-6).

Figure 2-6

Personnel Spending Falling to Four-Year Low



Sources: Expenditures and Authorities: *Public Accounts of Canada* 2009-10 to 2012-13, *Main Estimates and Supplementary Estimates* 2013-14 and 2014-15.

Overall personnel costs have fallen over the past four years, commensurate with a decrease in the number of public servants working in the core federal public service and separate agencies. As noted in an earlier PBO report, changes in employment levels are a key cost driver for overall personnel expenses.[8]

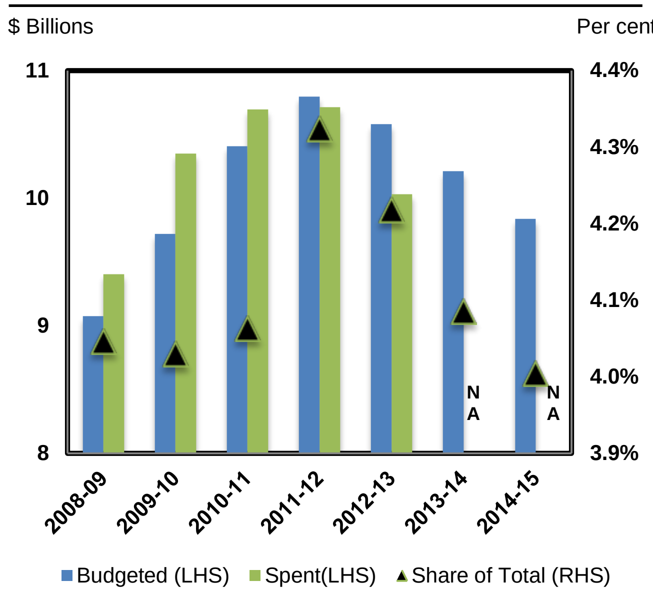
The decrease in personnel costs has been partially offset by one-time factors, such as the severance benefits for terminated staff and the elimination of voluntary separation benefits. With respect to the latter, the Government reports that its outstanding liability for *severance and other benefits* decreased $700 million in 2012-13 to $4.4 billion as of March 31, 2013.[9]

Professional and Special Services Costs

Professional and Special Services comprise the cost of payments made for specialized technical services (*e.g.* accounting, law, architecture), as well as other types of contracts, such as payments for veterans' care. In 2014-15 spending in this area is estimated to decrease $0.4 billion (3.6 per cent) to $9.8 billion (Figure 2-7).

Figure 2-7

Spending on Professional Services Returns to Pre-Stimulus Levels



Sources: Expenditures and Authorities: *Public Accounts of Canada* 2009-10 to 2012-13, *Main Estimates and Supplementary Estimates* 2013-14 and 2014-15.

[7] http://www.tpsgc-pwgsc.gc.ca/recgen/pceaf-gwcoa/1415/7-eng.html. Accessed March 2014.
[8] http://www.pbo-dpb.gc.ca/files/files/Federal_Public_Service_Wage_EN.pdf. Accessed March 2014.

[9] http://www.tpsgc-pwgsc.gc.ca/recgen/cpc-pac/2013/vol1/s6/rraaf-pofb-eng.html#sh13. Table 6.28. Accessed March 2014.

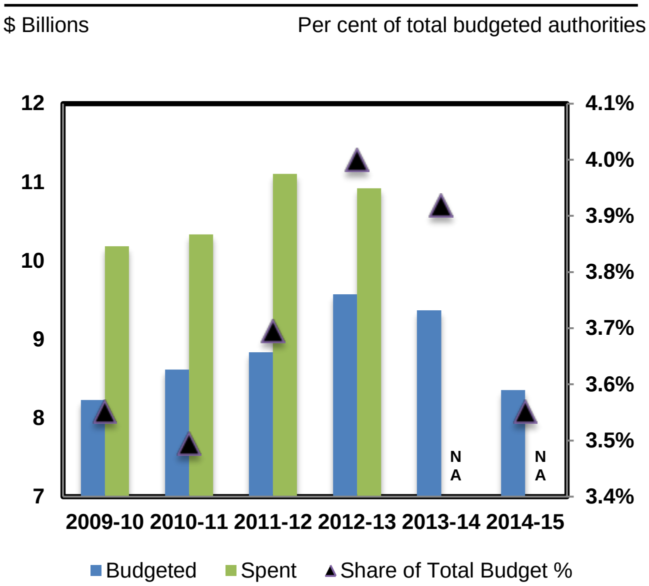
Spending on professional services as a share of the Government's overall spending grew temporarily as part of the stimulus package. For the coming fiscal year, it is now estimated to return to its historical share of total spending, approximately 4 per cent.

The Back Office

An area of spending that has a substantial planned decrease in spending is "Internal Services", which reflects the overhead and administrative cost of government operations (Box 2-8). In 2014-15 spending is estimated to fall $1.0 billion (10.8 per cent) to $8.4 billion (Figure 2-9).

Figure 2-9

Overhead Spending Continues to Fall



Sources: Expenditures and Authorities: *Public Accounts of Canada* 2009-10 to 2012-13, *Main Estimates* 2013-14 and 2014-15.

Note: Authorities and expenditures include total net spending by Shared Services Canada, which was established in 2011-12.

Internal Service spending as a share of total planned federal expenditures is projected to decrease to less than 3.6 per cent, close to its historical share.

Box 2-8

Calculating Internal Services

Virtually all federal departments and agencies have an "Internal Service" program, which according to the Government is a "group of related activities and resources administered to support the needs of programs and other corporate obligations of an organization".

The Government has never defined or explained how to calculate "back office", which was the primary focus of the Budget 2012 spending reduction package. As such, the PBO has tracked expenditures in this program to make inferences regarding trends in "overhead" spending – spending not directly related to front-line service delivery.

The PBO calculates Internal Service spending and authorities by federal organization, as follows:

- Actual spending is calculated for each federal organization using the total expenditure on the Internal Services program activity. An adjustment is made for net revenues, unless internal services are provided to another federal organization.

- Authorities information is sourced from the Main Estimates using a similar approach.

- As well, in 2011-12, funding was transferred from IT-related Internal Services across most departments and agencies to create Shared Service Canada (SSC). Hence, for 2011-12 onward net spending from SSC is also included.

Over three quarters of the planned decrease in spending is attributable to two organizations: National Defence ($478 million); and, the Canada Revenue Agency (CRA, $303 million).

As noted in earlier PBO reports, part of the decrease in the Government's overall planned spending reflects the reclassification of expenses previously considered "Internal Services" as other types of program expenses.[10]

3. Program Details

PBO's analysis focuses on those programs with the largest proposed changes in budgetary authorities, as measured by percentage growth or absolute dollars.

Consistent with the planned growth in major federal transfer payment programs to other levels of government and to individuals, two programs in these areas are responsible for the largest increases in spending: the Canada Health Transfer and Elderly Benefits. Spending on these two programs comprise over one quarter of the federal budget.

Canada Health Transfer

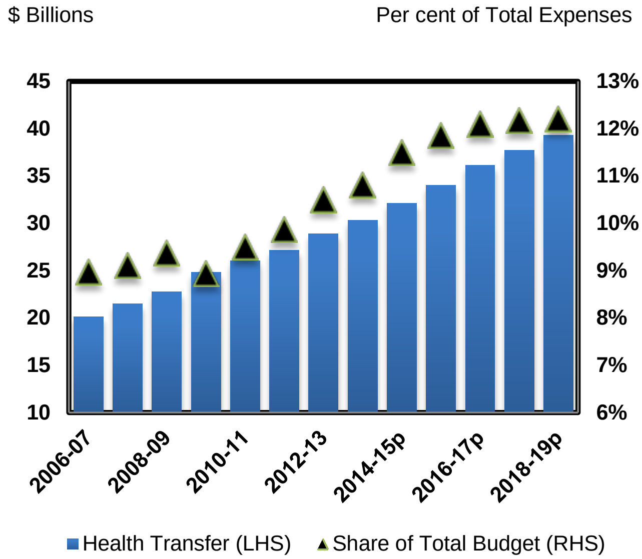
The Canada Health Transfer (CHT, part of Finance Canada's *Transfer and Taxation Payment Program*) is estimated to rise $1.8 billion (6.0 per cent) in 2014-15 to $32.1 billion (Figure 3-1).

The growth rate for the CHT is established in statute at 6 per cent per annum until 2016-17. Following that, the growth rate is benchmarked to a three-year moving average of the nominal GDP growth rate, with a minimum floor of 3 per cent per year.

CHT spending as a share of the total federal budget has grown from approximately 9.0 per cent in 2006-07 to 11.5 per cent 2014-15, and is projected to rise to 12.2 per cent by 2017-18.

Figure 3-1

Canada Health Transfer Spending Grows



Source: *Fiscal Reference Tables*; *Budget 2014*.

Elderly Benefits

Federal benefit payment programs for senior citizens are another important contributor to growth. In 2014-15, Elderly Benefits (part of Employment and Social Development's Income Security program) are estimated to rise $2.0 billion (4.8 per cent) to $43.8 billion (Figure 3-2).

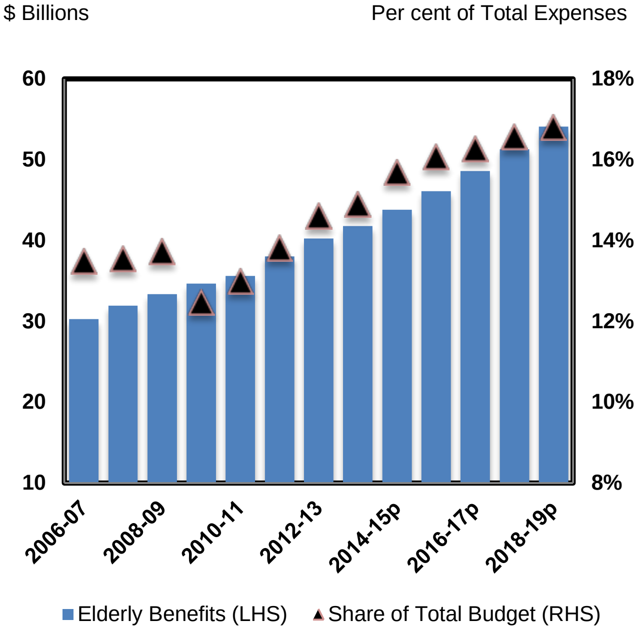
As noted in earlier PBO reports, the growth in Elderly Benefits is explained by two factors: the growing share of seniors in Canada's population; and, inflation (benefits are indexed to the Consumer Price Index).

Elderly Benefits as a share of the total federal budget are estimated to be 15.7 per cent in 2014-15, and are projected to grow to 16.8 per cent by 2018-19.

[10] http://www.pbo-dpb.gc.ca/files/files/Expenditure_Monitor_2013_14Q2_EN.pdf. Accessed March 2014.

Figure 3-2

Elderly Benefits a Growing Share of the Budget



Sources: Historical data from *Public Accounts of Canada*; Projections from *Budget 2014*.

Notwithstanding the overall decrease in estimated DPE compared to the previous year due to planned restraint, there are two areas of notable increase: National Defence's capital budget and the Communications Security Establishment's overall budget.

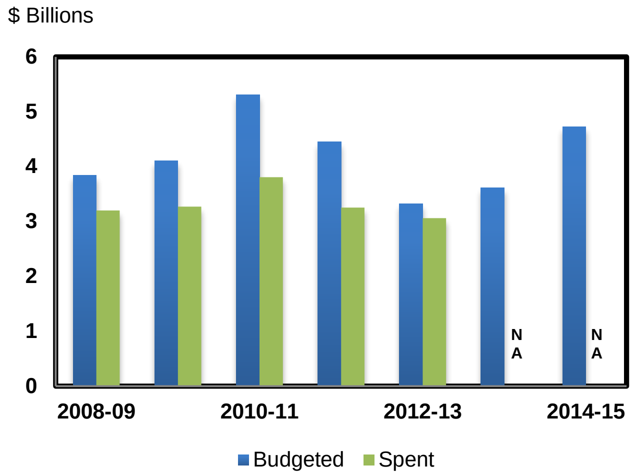
National Defence

National Defence's Capital Budget is estimated to grow $1.1 billion (or 30 per cent) in 2014-15 to $4.7 billion (Figure 3-3). If fully disbursed, this would be the highest level of annual capital investment in over a generation.

Budget 2014 indicated that funding earmarked for military procurements is being re-profiled to the medium-term as a result of delays (*i.e.* beyond 2017-18), but failed to identify which projects would be deferred. In contrast, the Government's Expenditure Plan indicates that the proposed funding increase is required to make "investments in major capital projects such as Land Combat Vehicles, Arctic Offshore Patrol Ships, Light Armoured Vehicle Reconnaissance Surveillance System Upgrade, and Canadian Armed Forces Health Services Centres."

Figure 3-3

National Defence's Budgeted Capital Spending Near Record High



Sources: Data prior to 2013-14 from the *Public Accounts of Canada*. Data from 2013-14 onward from the *Main and Supplementary Estimates.*

Communications Security Establishment

The Communications Security Establishment (CSE) was established as a standalone organization in 2012 from within National Defence.

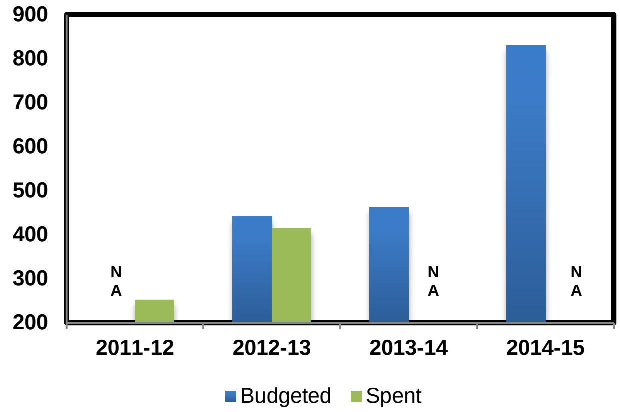
In 2014-15, CSE is seeking approval from Parliament to increase it's spending by $368 million to $829 million (80 per cent).

While the CSE does not publish a Report on Plans and Priorities or Departmental Performance Report, the Government's Expenditure Plan does provide some high-level information explaining the increase, which is attributed to the construction of a new headquarters and contract payments associated with its maintenance.

Figure 3-4

Communications Security Establishment Budgetary Authorities

$ Millions



Sources: Data from 2012-13 from the *Public Accounts of Canada*. Data from 2013-14 onward from the *Main and Supplementary Estimates*.