REFORMING FISCAL INSTITUTIONS IN CANADA

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1 Persistent structural deficits and the lead-up to the 1990s fiscal crisis

Canada experienced a fiscal crisis in the mid-1990s. The crisis came to a head due to a confluence of factors, but ultimately occurred because successive governments failed to address significant structural deficits that persisted for decades. Some statistics help convey the gravity of the problem: prior to balancing the budget federally in 1997, Canada ran 27 consecutive deficits (Figure 1). The PBO estimates that the federal government's structural deficit – which attempts to adjust for the fiscal impacts of the business cycle – averaged 5.3 per cent of GDP in the two decades prior to the crisis (Figure 2). With these large deficits, the federal debt-to-GDP ratio rose steadily over two decades, from 18 per cent in 1974 to a post-WWII high of 68 per cent in 1994. As government debt grew, so did public debt charges. At more than 6 per cent of GDP, debt charges represented 38 cents of every dollar in federal government revenue and increasingly crowded out the resources available to deliver public services.

Prior to the fiscal crisis, some partial corrective policy actions were taken that modestly improved the federal government's structural budget balance.[1] However, while government budget forecasts repeatedly predicted falling deficits in the early 1990s, these failed to materialize due to high domestic interest rates (aimed at reducing inflation) and the effects of a lingering recession. Concerns about the credibility of the government's forecasts eventually led to an external review (Ernst and Young, 1994). In addition, financial market's confidence in the ability of Canadian governments to resolve their fiscal problems was also eroding, as bond rating agencies downgraded the credit ratings of some Canadian sub-national governments.[2]

2 Mid-1990s fiscal consolidation and the emergence of budget surpluses

2.1 Fiscal consolidation

Canada's fiscal crisis prompted a decisive fiscal consolidation. While the 1995 Federal Budget is generally identified as a key turning point, many difficult and painful policy measures were taken in a short period of time, including wide-ranging policy reforms (Box 1). As a result, jurisdictions at the federal and provincial levels significantly improved their underlying fiscal positions. Table 1 reports the estimated change in the cyclically-adjusted primary balances (CAPB) of the Canadian jurisdictions with the largest fiscal improvements in the 1990s.

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This paper reviews developments in Canada's fiscal institutions – *i.e.*, budget processes conventions, constraints, and plans – and fiscal outcomes. The paper discusses Canada's institutional strengths and weaknesses, and identifies some potential areas for improvements in the context of current and looming fiscal challenges.

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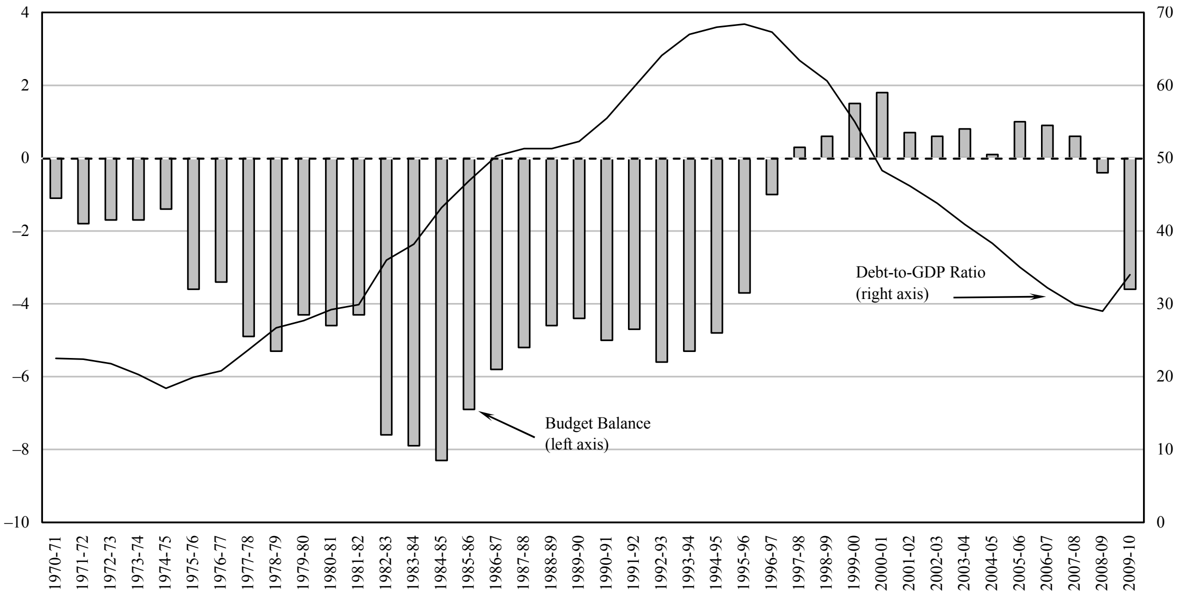
1 These actions included tax changes (partially de-indexing to inflation personal and corporate income tax credits) and the introduction of the Good and Services Tax; and the Federal *Spending Control Act* from 1991-95, which restrained program spending growth.

2 A confounding factor adding political uncertainty to Canada's fiscal problem was the potential for the province of Quebec to separate from Canada, which was only narrowly avoided in a 1995 Referendum.

Figure 1

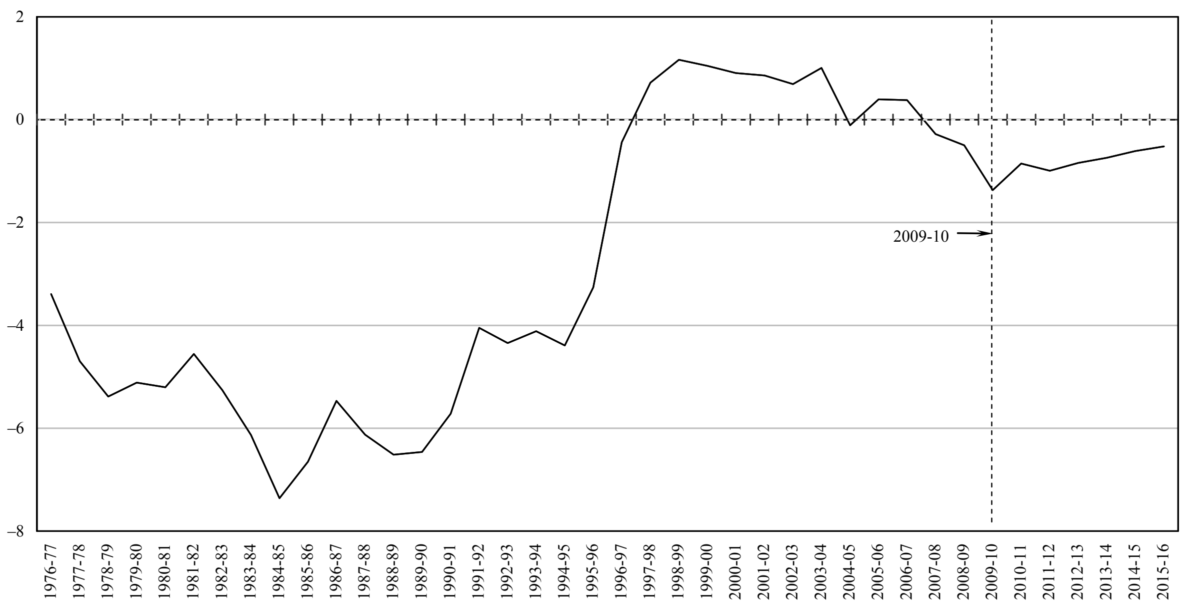
Canadian Federal Budget Balance and Debt-to-GDP Ratio
(percent of nominal GDP)



Source: Finance Canada Fiscal Reference Tables, October 2010.

Figure 2

PBO Estimates of Canada's Federal Government Structural Budget Balance
(percent of potential income)



Source: PBO (2010).

BOX 1
KEY FEATURES OF CANADA'S FISCAL CONSOLIDATION IN THE MID-1990s

- *emphasized spending reductions* over revenue increases, with roughly ¾ spending cuts versus ¼ revenues increases (Table 1);
- a federal *government program review*, which reduced public sector employment and involved large cuts in spending for some departments (e.g., transportation; natural resources; regional agencies; industry);
- *reduced and restructured federal-provincial transfers*, effectively down-loading some fiscal burden to the provinces (*i.e.*, a federal cost-sharing transfer for social services was reduced and changed to an unconditional block grant);
- *reformed social assistance* (welfare) in some large provinces;
- *restricted* the generosity of national *unemployment benefits*;
- actions to *make Canada's public pension plan* (CPP) *sustainable* over the long term (featuring steady increases to contribution rates);
- *privatized* some *public assets and activities* (e.g., federal air navigation); and
- *reduced* some *business subsidies* (e.g., transportation and dairy).

Table 1

Significant Fiscal Improvements
in Canadian Federal and Selected Provincial Governments in the 1990s

	Jurisdiction	Episode Timing	Δ CAPB	Of Which: Δ Revenue	Of Which: Δ Program Spending	Fiscal Rule
1	Newfoundland	1994-96	4.9	0.8	–4.0	
2	Saskatchewan	1993-94	4.8	0.6	–4.3	BB 1995; D 1995
3	Nova Scotia	1993-96	4.7	1.9	–2.9	S 1993; BB 1996
4	Federal	1995-98	4.5	1.3	–3.2	S 1991; BB targets 1994
5	Ontario	1993-96	4.1	0.8	–3.3	BB adopted 1999
6	Alberta	1993-94	4.0	0.9	–3.1	S 1992; BB 1993; R 1995; D 1995
7	Manitoba	1993-95	3.6	0.9	–2.6	BB 1995; R 1995; D 1995
8	Quebec	1995-99	3.4	0.7	–2.8	BB 1996
	Average		**4.3**	**1.0**	**–3.3**	

Sources: PBO (2010a); OECD (2010).
Notes: CAPB is the cyclically-adjusted primary budget balance. These episodes featured an improvement of at least 3 percentage points in the CAPB as a share of potential GDP, sustained over 2 years. In fiscal rule column: S represents a spending rule; BB a budget balance rule; R a revenue rule; and D a debt rule. Columns may not sum due to rounding.

In addition to policy changes, there were important changes to Canadian budget processes based on the review of the federal government's budget forecasts and fiscal consolidation plans, including:

- an *increased use of fiscal rules* to constrain discretion: both legislated and non-legislated targets were used by the federal government and many provinces.[3] PBO analysis finds these targets likely played a supportive role in achieving, or attempting to lock-in, fiscal improvements in many of the largest Canadian consolidations in the 1990s (PBO, 2010a).[4]
- an *attempt to increase the distance between the federal government's forecasts and the political process* by basing the government's economic assumptions on a private sector survey rather than the government's internal forecast.
- *basing budget forecasts on prudent assumptions* in two ways: 1) by adding explicit bottom-line contingency reserves and prudence factors; and 2) by making more fiscally prudent economic assumptions than the private sector survey average (e.g., assuming higher interest rates and lower economic growth).
- *some increases in budget transparency*: the federal government began releasing mid-year updates on the economy and its budget forecast.

2.2 The emergence of budget surpluses and deficit-avoidance

With these policy actions and budget processes changes, Canada's public finances quickly improved in the late 1990s and into the first decade of the 2000s. Indeed, the mid-1990s fiscal crisis had changed the landscape for Canadian fiscal policymakers and it was now expected that Finance Ministers across Canada would balance their budgets. Deficit avoidance was the order of the day as the political cost of a deficit was high. Canada recorded 11 consecutive surpluses federally (1997 to 2007), which averaged a little less than 1 per cent of GDP. Federal debt-to-GDP ratio fell from 68 per cent in 1995 to 29 per cent in 2008. Public debt charges as a share of revenue similarly fell from 38 per cent in 1990 to 13 per cent in 2008. Canada's international standing was also much improved, moving from one of the worst fiscal positions in the G-7 in the mid-1990s, to being the leader (Figure 3).

Despite this success, there were fault lines developing beneath the surface, as some of the responses to the 1990s fiscal crisis created their own problems. As persistent deficits turned to persistent surpluses, pressure mounted to spend the "fiscal dividend" and lower taxes rather than, or in addition to, reducing public debt. As a result, during expansionary times, taxes were cut (e.g., personal and corporate taxes, and the national value-added tax GST) and program spending, which had been temporarily cut or had its growth slowed, eventually ramped back up. By the time the global financial crisis hit in 2008, structural deficits had re-emerged in Canada (Figure 2).

For several years, despite sizable in year policy measures, the federal government under-estimated the surplus. In attempts to avoid having all excess fiscal room applied to debt repayment, as required by accounting rules, the government made one-off transfers to provinces and

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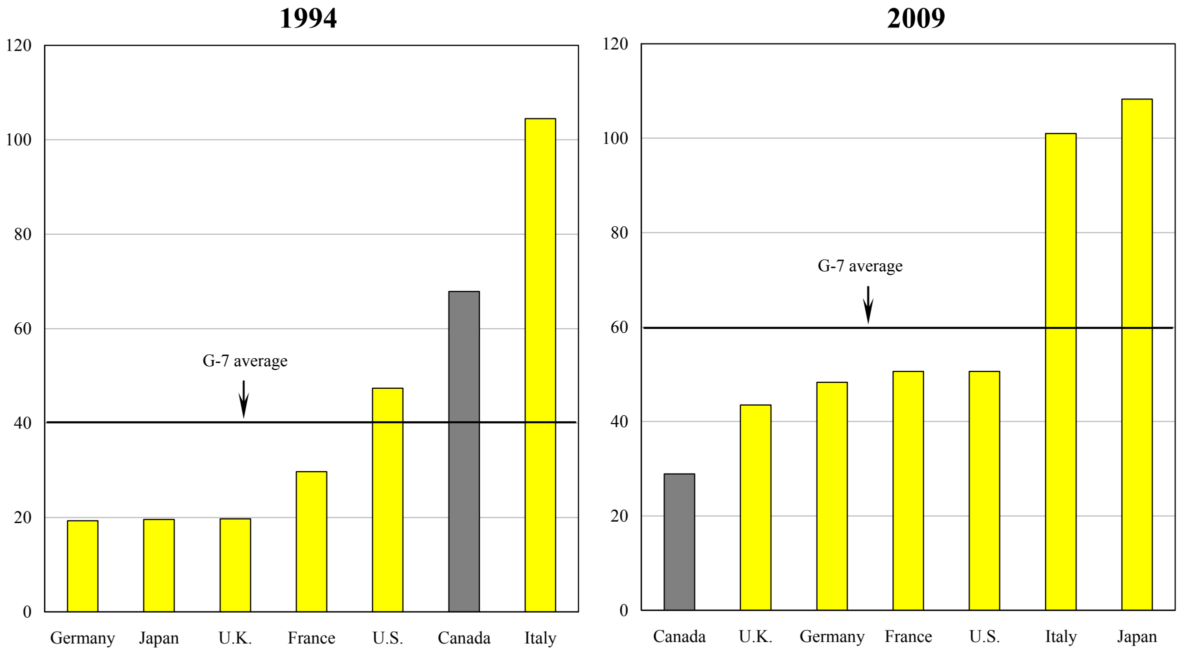
3 While the federal government introduced short-term deficit and budget balance targets, many provinces introduced balanced budget legislation. The federal government began with an interim 3 per cent of GDP deficit target by 1996-97, which later became a target to balance the budget or achieve a surplus. Later specific debt-to-GDP ratio targets over the medium- and longer-term were also chosen. Some provinces used legislation to: limit spending; restrict tax rate increases; and require debt management strategies to lower debt-to-GDP ratios and build up stabilization funds in economic expansions which could subsequently be drawn-down in recessions.

4 There were, however, significant differences across jurisdictions in governments' abilities to follow their rules and improve their finances. This suggests that fiscal rules on their own cannot be relied on to improve a government's finances and that other factors are also needed such as: clear policy goals; political will; public support; and a strong budget framework and reporting practices.

Figure 3

G-7 General Government Net Financial Liabilities
(percent of GDP)



Source: Finance Canada Fiscal Reference Tables, October 2010.

arms-length foundations – where the latter were not under the preview of Parliament.[5] These actions made discretionary fiscal policy pro-cyclical, less predictable and were generally seen as inhibiting debate regarding how additional funds should be allocated.

In 2005, with the surplus under-estimated in eight of the previous nine years, the credibility of the federal government's budget forecasts were again questioned, resulting in another external review (O'Neill, 2005). This review found that the government's forecast had been padded with implicit prudence, over and above the explicit bottom-line contingency reserves. This result was attributed to the annual no deficit target that had emerged, which gave incentives for those producing the fiscal projections to incorporate extra prudence into their forecasts (persistently under-estimating revenues and over-estimating program spending). Finding fault with the fiscal target more than the forecasting process, O'Neill recommended the federal government change its annual budget balance target to instead aim for a surplus, on average, over the economic cycle (as is done in Sweden for example). The rationale was to shift the focus of budget planning away from short-term annual results toward a more medium-term perspective, and to move away from strict deficit avoidance towards the avoidance of *structural* deficits (which would allow for deficits in recessions).[6]

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[5] Between 1997, the year the budget was balanced and 2004, more than $9 billion was transferred to foundations. Auditor General (2005) details the concerns about a lack of accountability (e.g., no performance reports to Parliament and ineffective Ministerial oversight).

[6] The recommendation to change the annual budget balance target was dismissed, and instead, the government proposed (in 2005 but did not pass) legislation that would allocate any unanticipated surplus. The legislation would have allocated any surplus in excess of the $3-billion contingency reserve (which applied directly to debt reduction at year-end) in the following manner: 1/3rd to spending; 1/3rd to tax relief; 1/3rd to debt repayment.

In addition to the larger-than-expected surpluses, public concerns were raised and political debates waged about cost overruns on federal projects (e.g., a new firearms registry program) and a general lack of financial transparency about the cost of programs and proposed legislation. A key argument forwarded was that more financial due diligence by parliamentarians before implementation, possibly with assistance from independent financial experts, might have minimized these cost overruns. At the same time, parliamentarians indicated they had insufficient support to hold the government to account because they required more expertise and resources to assist them in scrutinizing the government's budget projections and estimates (*i.e.*, appropriations).[7]

3 Recent developments in fiscal institutions

3.1 The creation of Canada's parliamentary budget office

In 2006, a new minority conservative government was formed, which brought in a series of measures under the *Federal Accountability Act*.[8] This *Act* created the Parliamentary Budget Officer (PBO), whose mandate can be viewed as an institutional change that attempts to address some of concerns described above. The PBO's mandate as outlined in legislation is to provide independent analysis to Parliament on the state of the nation's finances, the government's estimates (appropriations) and economic trends, and upon request, to estimate the financial cost of matters under Parliamentary jurisdiction. The legislation also includes a provision granting the PBO timely access to the government's economic and financial information.

The PBO began its operation in 2008 and has prepared a number of reports in each area of its mandate that have engaged parliamentary debate, including:

- *State of the nation's finances:* independent budget projections; estimates of the federal government's structural budget balances; budget balance risk analysis (fan charts) and a long-run fiscal sustainability report.
- *Estimates review:* Expenditure analysis tracking the implementation of fiscal stimulus measures including: impact assessment; reporting standards; flow of funds analysis; and lapse forecasting as well as reports on the risk associated with the government's spending restraint.
- *Economic trends:* analysis on a range of issues including: Canada's output gap; labour markets; current economic indicators; Canada's experiences with fiscal rules and consolidations; and the risk of deflation.
- *Financial analysis:* costing of a range issues including: Canada's military engagement in Afghanistan; Aboriginal education infrastructure; crime legislation; military procurement; G8/G20 meeting security; and several Private Member Bills.

During its first few years of operations, the PBO has had a bumpy experience. This has included budget reductions after the release of controversial reports (on the costs of Canada's engagement in Afghanistan and economic and budget projections during the global financial crisis of late 2008) and a subsequent budget reversal with a Parliamentary Committee review of its operations.[9] Nonetheless, the PBO has had an impact and pushed the government to improve its

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[7] Parliament's most recent comprehensive review of the estimates was undertaken in 2003 by the House Standing Committee on Government Operations and Estimates. At that time, the Committee noted that "while parliamentary committees were intended to be bodies where detailed scrutiny of government spending and performance would occur, this was not being done".

[8] The *Federal Accountability Act* dealt with lobbying and conflict of interest rules, restrictions on election financing and measures respecting administrative transparency, oversight and accountability.

[9] A main issue of the PBO review was the office's open publishing model – *i.e.*, openly publishing all of its reports on a public website – an media visibility. This approach challenges a convention of confidentiality and Parliamentary ownership of requested analysis.

transparency. To provide a few concrete examples: the PBO's independent cost estimates have resulted in the government making public (and in some cases significantly adjusting) its estimates of the costs of various legislation and policy measures; the government has abandoned its booking of budgetary revenues from the unspecified future sales of corporate assets after the PBO disputed such claims; and the government has been required to release some details underlying its budget projections that the government had not provided, but had previously been public.

Despite these modest successes, major challenges remain for the PBO. One concern is that the PBO's resources (annual budget of $2.8 million and staff of 14) are insufficient to effectively fulfill its legislated mandate – particularly scrutinizing appropriations. Second, the PBO has been given limited access to government information (highlighted by the government's repeated use of 'Cabinet confidence' to restrict information flow), despite a legislated information provision. Finally, the PBO has had its independence limited by external administrative controls by its inclusion within the Library of Parliament (rather than being an independent office) and a flawed appointment process (the PBO is appointed and works at pleasure for the Prime Minister).

3.2 Comparison with other newly-created independent fiscal agencies

While the main change to fiscal institutions in the 1990s was a move towards fiscal rules, more recently there has been increasing interest and experimentation with independent fiscal institutions as a means to improve fiscal policy making and budget transparency and to complement fiscal rules (Box 2). Such agencies have been advocated by the IMF, OECD and the European Commission. Since 2007, a "second-generation" of fiscal councils has been established in Sweden, Canada, Hungary, the U.K., and Slovenia.

Despite their distinct country-specific situations and mandates, these organizations, like the PBO, have generally experienced a variety of implementation difficulties, ranging from: inadequate resources (Hungary's council was significantly reduced in 2010 after suggesting the government's budget lacked transparency and its assumptions were too-optimistic; similar budget cuts were threatened for Sweden's Fiscal Policy Council after public debates over the appropriate degree of fiscal stimulus); to government criticism of the agency's findings; to concerns about the independence of budget forecasts (in the case of the U.K's Office for Budget Responsibility which relies heavily on Treasury resources).[10]

4 Canada's current economic and fiscal context and looming challenges

4.1 Current context

The 2008 global financial crisis brought about a recession in Canada, which was met with a significant easing of monetary policy and fiscal stimulus. Despite the external nature of the shock and the resilience of Canada's financial institutions, the impact on the economy and the government's fiscal situation has been significant. The PBO estimates that Canada's output remains roughly 3 per cent below potential, and given the modest recovery forecasted, this suggests that the output gap may not close before 2016 (Figure 4). This is the average or mean economic outlook, but the risks are weighted to the downside. Key risks including: the fragile nature of the U.S. recovery, reflecting the continued weakness of households and the labour market; recent political turmoil in the Middle East, which has exacerbated rising commodity prices; sovereign

[10] For more on international fiscal institutions and case studies of Sweden's and the U.K.'s experiences, see Calmfors and Wren-Lewis (2011) and Calmfors (2011).

BOX 2
SOME ROLES AN INDEPENDENT FISCAL AGENCY CAN PLAY

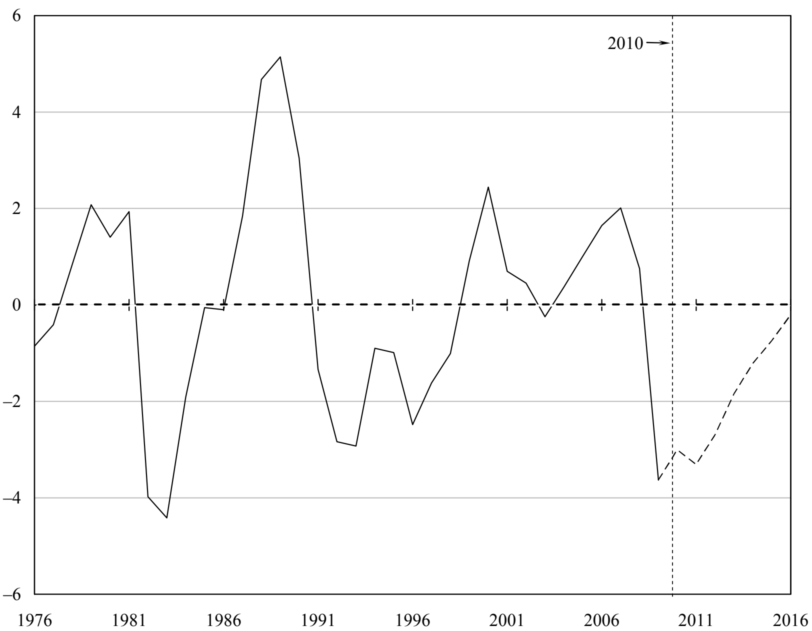
- *Monitoring* – In the context of fiscal rules and budget targets, a fiscal agency can play a key role in oversight by serving as an independent monitor by analyzing whether the government's fiscal policy has achieved or will likely achieve its key objectives. As another example, a fiscal agency can help assess whether the government's fiscal plan is based on prudent forecasting assumptions.
- *Provider of long-run economic and budget analysis* – To the extent that the political process may place too much emphasis on the near-term and too little emphasis on future generations, a fiscal agency can provide regular analysis of the long-run sustainability of the government's fiscal position, and the sensitivity of the results to alternative assumptions.
- *Actor to improve budget transparency* – To the extent that there is insufficient budget information and understanding in the public domain, a fiscal agency can play a key role is in the public provision of budget information in order to improve budget transparency.
- *Provider of financial analysis and costing* – To support Parliamentary decisions on legislation and large-scale policy initiatives, a fiscal agency can provide financial analysis and cost estimates.

debt concerns and heightened currency tensions on international markets, which could ultimately raise risk premia and global interest rates; Canada's high level of household debt, which could restrain domestic consumption; and the appreciation of the Canadian dollar, which could hinder Canada's net exports.

In light of these heightened economic risks, an unwelcome fiscal planning development is that since 2009, the federal government has abandoned its use of bottom-line, back-end-loaded contingency reserves that grow over the forecast horizon. Instead,

Figure 4

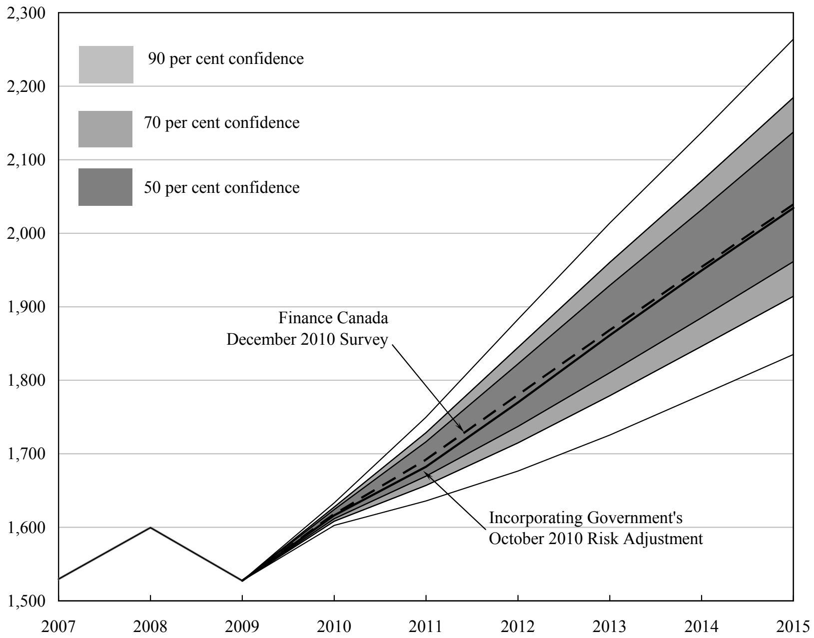
PBO Estimates of Canada's Output Gap
(percent of potential GDP)



Source: PBO (2011), Statistics Canada.
Notes: Based on Finance Canada's December 2010 survey and PBO's estimate of potential output.

Figure 5

PBO Fan-Chart Nominal GDP Forecasts
(billions of dollars)



Source: PBO (2011), Statistics Canada.

they have opted for minor (front-end-loaded) downward adjustments to nominal GDP in the short-term, relative to the private sector survey average. Figure 5 demonstrates that the size of this most recent adjustment has been trivial, and does not materially represent a more prudent basis for planning than the private sector survey – the approach that was followed in the late-1990s.

Canada's fiscal position has been thrown off track and, absent further policy actions, is likely to remain in deficit over the medium-term. In other words, as a result of the tax cuts and spending increases over the past decade, modest structural deficits have re-emerged in Canada (Figure 2). The PBO estimates that nearly $200 billion will be added to Canada's federal debt between 2008 and 2015. The federal debt-to-GDP ratio is projected to rise to 35 per cent in 2011 before falling, based on the relatively favourable private sector average forecast assumptions. To quantify and illustrate how economic risks affect the fiscal projection, the PBO constructs "fan charts". Figure 6 shows the range of status quo budgetary balance outcomes from PBO's February 2011 projection, which estimates only a small probability of achieving budget balance by 2015.

Canada's fiscal planning environment is part of a broader international shift in fiscal policy that is currently underway, moving from winding down stimulus measures towards constructing and implementing fiscal consolidation plans. While the need for fiscal consolidation is real – and significantly larger in many countries outside of Canada – getting the timing right will be difficult, so as to not upset the economic recovery. As in several other countries, consolidation plans in Canadian jurisdictions remain inadequate and largely incomplete, relying mainly on unspecified spending restraint. Indeed, fiscal transparency in general remains a key concern. Furthermore, clear objectives and policy guidance are largely absent as several of the fiscal rules and targets of Canadian federal and provincial government's have been temporarily abandoned or their status remains unclear (PBO, 2010a).

An additional complication that will arise in the next few years is a looming deadline to renew large federal-provincial health and social transfers and Equalization agreements (the Equalization program transfers funds across the provinces). Casting a shadow over these challenges is a minority federal government political context that is largely short-term focused and appears to lack the required political consensus needed to put Canada on a solid footing for the future.

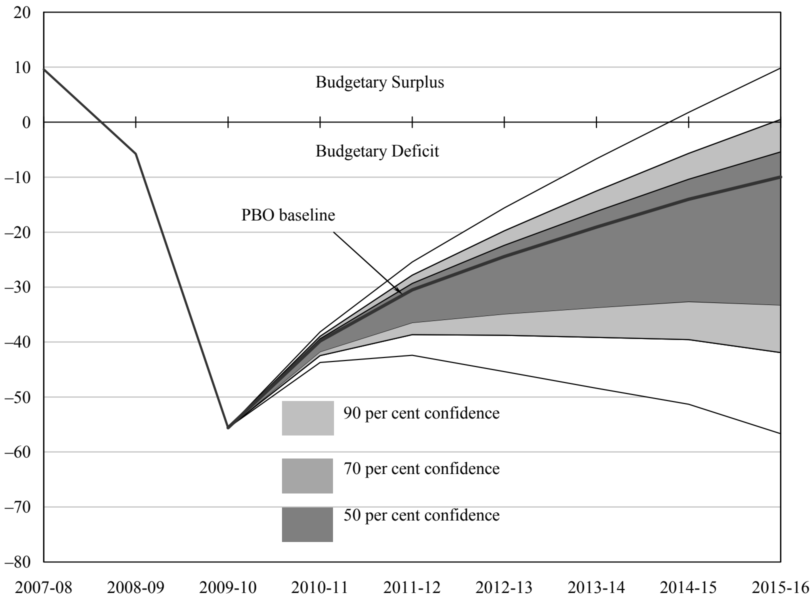
4.2 Looming long-term challenges

Analyzing the sustainability of government finances requires a longer-term perspective, well beyond the current budget planning cycle. In Canada, as in other industrialized countries, a major demographic transition is underway that will strain government finances. During this time, population ageing will move an increasing share of people out of their prime working-age and into their retirement years. Figure 7 shows PBO's long-term projection of Canada's old age dependency ratio (*i.e.*, the population aged 65 and over, divided by the population aged 15-64). Currently, for every person aged 65 and older there are just under five people of working age; by 2020 this is expected to fall to roughly 3.5 people; and by 2050 to just over two people. With an older population, spending pressures in areas such as health care and elderly benefits are projected to intensify. At the same time, slower labour force growth is projected to restrain growth in the economy, which will in turn slow the growth of government revenue.

The PBO's long-term fiscal sustainability analysis brings these demographic and

Figure 6

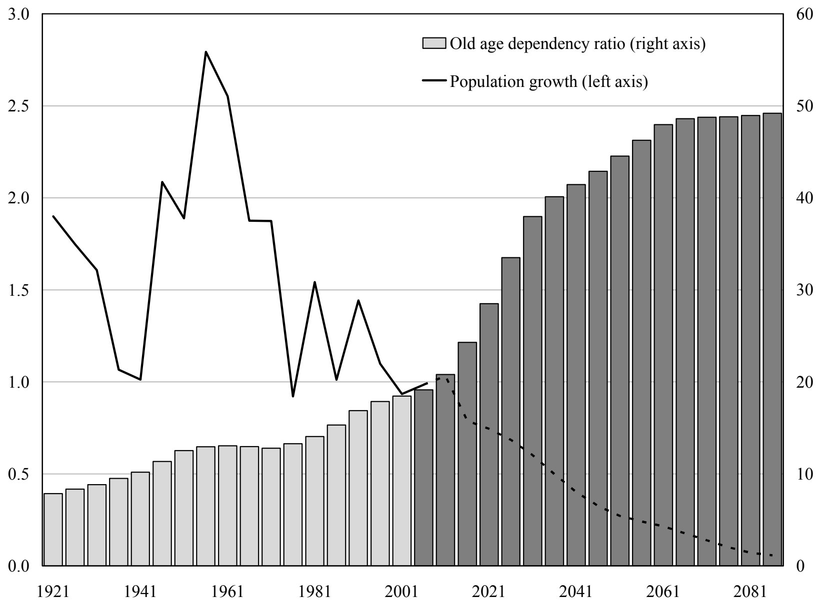
PBO Fan-Chart Budget Balance Projections Given Economic Uncertainty and Downside Risk
(billions of dollars)



Source: PBO (2010b), Finance Canada.

Figure 7

Population Growth and Old Age Dependency Ratio Projections



Source: PBO (2010b).

economic projections together into a coherent quantitative framework. This work estimates a fiscal gap of around 1-2 per cent of GDP at the federal level – where the *fiscal gap* is the permanent improvement in the primary balance by tax increases and/or spending reductions required to stabilize the debt-to-GDP ratio (PBO 2010b).[11]

Weak productivity growth is another key long-term policy challenge in Canada, where labour productivity growth has averaged only 1.2 per cent annually over the last 30 years. More troubling is that, over the past 10 years despite a number of policy measures to boost labour productivity, its growth rate has fallen to only 0.8 per cent annually.

5 A path forward

5.1 Advice for establishing an effective independent Budget Office

In our opinion, Canada has made some modest progress recently with the establishment of a legislated budget office, but there remain some key challenges and missed opportunities. The difficult shared experiences of the PBO and other "second-generation" budget offices, suggests the following advice to other countries that are considering creating an independent fiscal agency:

It is imperative to establish the office properly from day one. This means getting the legislation right and hiring the best people because correcting initial mistakes is extremely difficult (or as some senior officials put it to us, "cement dries quickly"). Adequacy of long-term resources and funding and a legislated information provision with consequences for non-compliance are also essential ingredients, as are safeguards for the office's independence from political interference. In this regard, it is particularly noteworthy to compare the unquestioned independence typically afforded to monetary policy institutions, relative to the minimal protections given to newly-created fiscal policy agencies, whose tasks are at least as politicised and controversial. The appointment process and administrative relationships with legislature and executive should be clear and free from potential conflicts of interest. At the PBO, our experiences suggest that a small office can have a disproportionate impact in a short period of time, but lasting progress will ultimately require systemic cultural change within government towards transparency.

5.2 Some principles to improve Canada's fiscal institutions

The following are a set of basic principles to help improve Canada's fiscal institutions, including taking a prudential approach to fiscal policy:

- *Base budget plans on prudent assumptions and have explicit (not implicit) contingencies:* Risk is a four-letter word. Nonetheless, we need to acknowledge risk and the inherent and unavoidable uncertainty of fiscal planning. While Canadian budgets often discuss the sensitivity of their budget projections to changes around central assumptions, none currently used "fan charts" to quantify risk. In our view, attempts to analyze and quantify risk by reporting confidence intervals around budget forecasts and initial costs estimates for major policy proposals and legislation are essential. The reason to quantify risk is to provide governments with guidance to set aside appropriate and explicit risk provisions – as we have learned from experience, implicit risk provisions inhibit budget transparency and debate and can erode the credibility of government budget forecasts. In this area, recent federal budgeting changes which make superficial short-run adjustments to nominal GDP erroneously convey the illusion of real risk-adjustment, but are clearly insufficient, particularly compared with previous approaches in deficit times.

[11] The fiscal problem may be even larger for some provinces, given that the provinces bear the main responsibility for health spending.

- *Focus on fiscal crisis prevention:* Canadians have learned the hard way that it is better to avoid a fiscal crisis than be forced into a large and painful consolidation. Embedding in our fiscal institutions forward-looking frameworks and/or rules that help restore and preserve fiscal sustainability can improve economic stability and growth and promote inter-generational fairness.
- *Set clear, measurable policy goals at varying time horizons to provide policy guidance and allow progress to be monitored:* Independent fiscal agencies can play a monitoring role in *ex ante* and *ex post* compliance. For example, fiscal projections and plans should provide sufficient details, milestones, and measurable objectives to allow Parliament to hold the government to account.
- *Use structural budget balance estimates for medium-term planning:* Canadian governments should publish estimates of their structural budget balances over their forecast planning horizons to improve understanding and debate; surprisingly none do so at the current time. While such a tool is imperfect, failure to use structural balances means: one cannot operationalize a structural budget balance target (as advocated by O'Neill (2005), for example); one cannot distinguish cyclical from structural fiscal trends – an issue particularly important at turning points in the cycle or when the economy is above potential and temporary cyclical fiscal room can be mistaken for permanent fiscal room; and finally, one cannot assess whether the degree of fiscal consolidation is sufficient to restore budget balance in more normal times.
- *Increase the use of long-term strategic economic and budget analysis and planning:* Despite important long-term fiscal challenges and legislated requirements in other countries, few budgets in Canada include long-term fiscal analysis, plans or priorities. The political process generally puts too little weight on the impacts of current policies on future generations. Budget processes, therefore, need to be reformed to ensure an effective management of the nation's finances on a long-term basis. This could include annual fiscal sustainability calculations that are legislated, and possibly conducted by an independent budget office. Such analysis is essential for effective fiscal management.
- *Improve budget transparency:* In this area there is glaring gap between what was promised in the legislation and what is being delivered. The PBO's legislation contains an information access provision, yet requests are routinely denied and even previously public government information (e.g., details of budget forecasts and cost estimates of major programs) has been declared a "Cabinet confidence". Either legislation or convention should require public government costing on major legislation or policy initiatives. Furthermore, the full range of program activities across government including strategic reviews should be examined by Parliament and supported by quarterly financial reporting to track in-year spending. Such analysis should be made public whether conducted by the government or an independent legislative budget office. This would allow independent scrutiny of the analyses and enhance their credibility. Without budget transparency, accountability and informed public debate are hindered.
- *Return to Westminster roots:* Parliament's fiduciary role over the control of government funds needs to be re-affirmed. Parliamentary scrutiny of appropriations must become a core and time intensive activity – particularly in the context of spending restraint and strategic reviews.
- *Beware of flattery and false comparisons*: Canada's strong relative fiscal position internationally makes complacency and policy inaction a real risk. The appropriate metric, however, is not relative international rankings; it is public finances that are sustainable over the long-term. By this yardstick, Canada has work to do. We must not let our narrative of success through the global financial crisis prevent necessary reforms. Being less unsustainable than other G-7 governments must not be good enough for Canadian fiscal policymakers. Actions are required.

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