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A Tale of Two Provinces: Spending Overruns in Ontario and Quebec Spell Fiscal Trouble

By Yvan Guillemette and William Robson

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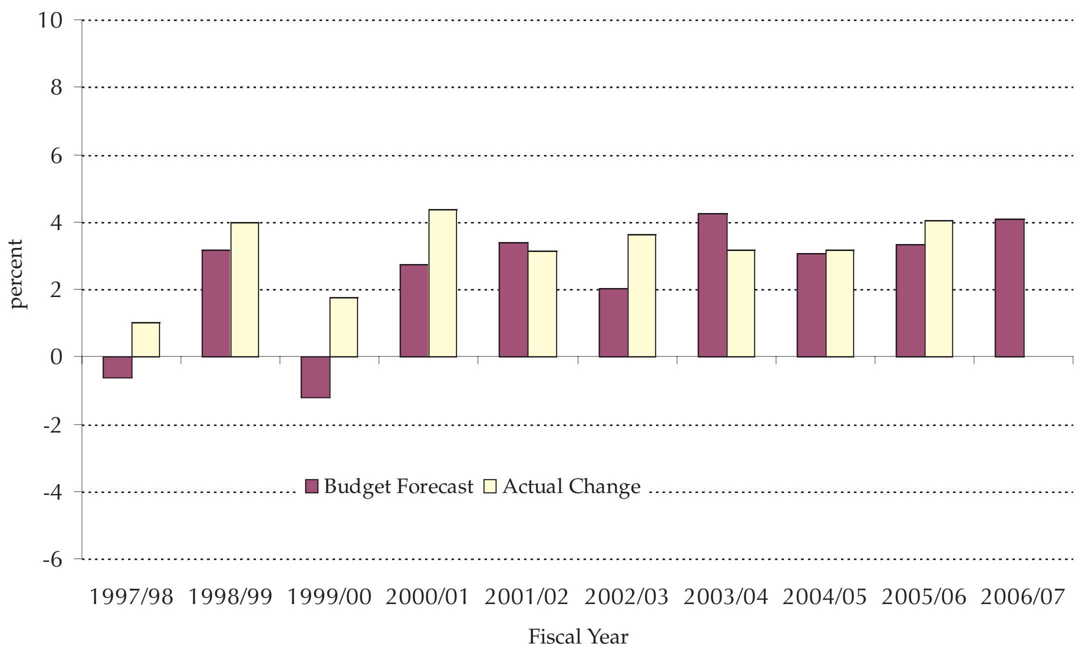
The simultaneous delivery of provincial budgets in Ontario and Quebec this spring provided a useful chance to see how governments of two key provinces faced with similar challenges are responding. The focus of budgets, and commentary on them, tends to be forward-looking. But before putting faith in the forward-looking elements, budget-watchers should ask what this year's numbers reveal about the reliability of budget commitments in the past.

The short answer is that, in recent years, one-year-ahead budgetary spending forecasts have been much more reliable in Quebec than in Ontario. Over the past decade, both provinces have tended to spend more than projected. While Quebec's record has improved to the point where its citizens can have some confidence that this year's budget commitments are serious, Ontario continues to overrun its commitments by large margins. Ontarians are therefore entitled to take their government's latest promise to control spending with a large grain of salt.

Like all provinces, Ontario and Quebec are struggling with aging infrastructure and relentless pressure to spend on health. Canada's two largest provinces, in particular, are on the wrong side of the shift in global patterns of supply and demand that has driven prices for natural resources up relative to those of manufactures. How effectively the two central provinces respond to the economic challenges of competition in their core industries and a resource-price-supported Canadian dollar matters to their citizens and to Canadians elsewhere. There is much in the recent performance of both to cause concern. They lag the country as a whole in growth of output and employment. Their tax systems discourage work and — particularly in Ontario's case — investment, more than those in most other provinces and nearly any other country (Mintz et al. 2005). And recent trends in capital investment by businesses — a critical force behind rising living standards — bode ill for the future: workers in Ontario get only about 65 cents of new plant and equipment each year for every dollar received by their US counterparts, and those in Quebec get less than 50 cents (Goldfarb and Robson forthcoming).

Figure 1: *Year-to-Year Change in Quebec Government Budgetary Expenditures*



Sources: Provincial Budgets and Public Accounts.

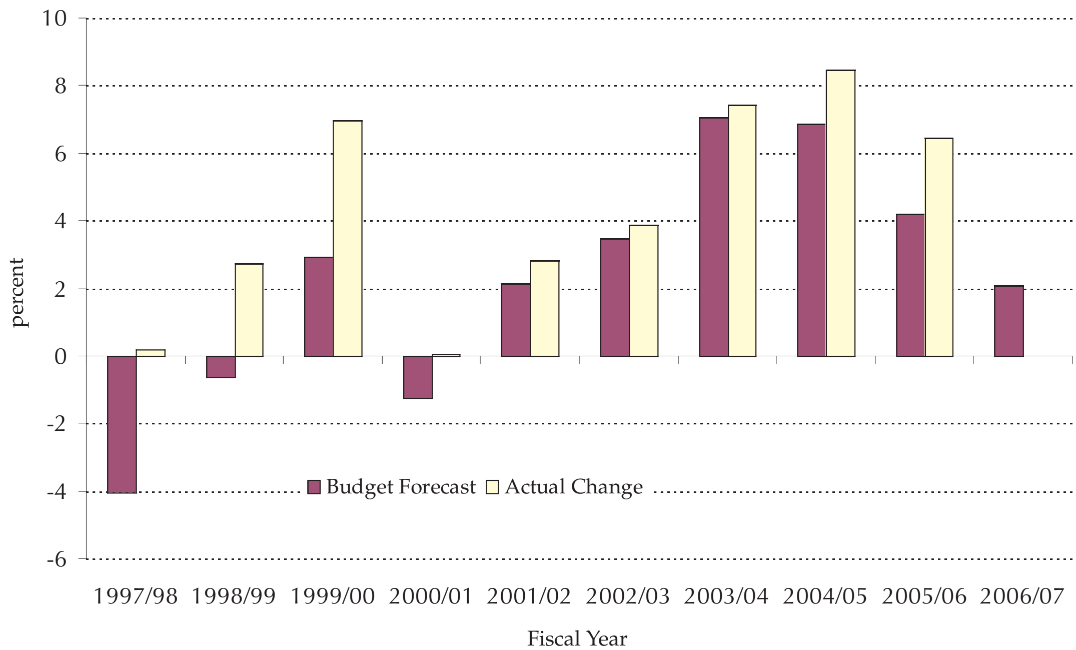
Notes: To reduce the impact of changes in accounting that would distort a comparison of levels of projected spending in annual budgets with levels of spending as shown in the most recent public accounts, we compare the projected change in program spending in each year's budget with the change recorded in the public accounts for that same year. Public accounts figures for 2005/06 will not be available until the fall; the "actual" figures shown for that year are from the 2006 provincial budgets.

Many fiscal steps that could improve this performance are no mystery. Both provinces need to improve their attractiveness as places to live and work. They need to control debt, so the taxes people pay fund more services and less interest. They need to keep their tax rates competitive. An essential precondition for all these priorities is controlling program spending — a task that deserves particular attention from parliamentarians, since they control program spending more than they control annual tax yields and interest rates. Money bills determine whether governments stand or fall.

At the level of rhetoric, and in the presentation of fiscal plans each year, the governments of Ontario and Quebec have repeatedly acknowledged the importance of discipline in spending. Members of the Ontario legislature and the Quebec National Assembly who supported their governments' budget legislation in recent years might reasonably have thought they were endorsing prudent plans — not just because of the rhetoric, but also because the spending plans for each successive fiscal year generally looked restrained.

If actual results had matched the proposals legislators saw at budget time, however, the fiscal situations of the two provinces would now be very different. The past nine years of budget projections and actual spending increases recorded at the end of each fiscal year in Quebec appear in Figure 1. In seven of those years, the Quebec government overshot its budget-time commitments. The average

Figure 2: *Year-to-Year Change in Ontario Government Budgetary Expenditures*



Sources: Provincial Budgets and Public Accounts.

overrun over the period was 0.9 percent of projected spending. In dollar terms, total projected annual increases since fiscal year 1997/98 came to $10.2 billion; actual spending increases came to $14.0 billion. In other words, for every dollar the Quebec government promised to raise program spending, it actually added a further 37 cents.

Figure 2 shows projections and out-turns for Ontario in the same fashion. If Quebec's overall record of meeting commitments is bad, Ontario's is far worse. In each of the last nine fiscal years, Ontario overshot the increase in spending projected at budget time. The average overrun during the period was 1.8 percent of projected spending. In dollar terms, the total projected change since 1997/98 was $15.0 billion; the actual was $26.4 billion. For every dollar Ontario pledged to increase programs, it added a further 76 cents.

Both provinces saw changes in government in 2003 — Quebec in April, Ontario in October — so it is natural to ask whether their recent fiscal performances have improved over what came before. In Quebec, the answer is yes. From 2003/04 through 2005/06, Quebec's cumulative record is virtually spot on — in fact, the total increase in spending has been some $0.2 billion less than budgeted. In Ontario, on the other hand, the overrun in 2004/05 was 1.6 percent, and the overrun in 2005/06 is currently estimated at 2.3 percent. The overrun in those two years alone is $2.9 billion — equal to the provincial deficit for this period.

The importance of presenting parliaments with realistic projections at the beginning of the fiscal year is hard to overstate. Budget time is the one occasion when key choices between priorities that require planning and action in advance are possible with a clear view of the tradeoffs. Even people who do not favour debt pay-down or lower taxes should not accept persistent gaps between what the governments commit to at budget time and what they actually deliver.

If the public accounts for 2005/06 bear out the figures presented in the National Assembly on March 23, Quebec has entered a new era of fiscal accountability, in which the spending projections in each year's budgets are a reliable indicator of what will actually occur. That would be a key first step in improving Quebec's fiscal competitiveness and addressing its economic challenges. In Ontario, by contrast, people have little reason to believe that the modest 2.1 percent increase in spending projected in the 2006 budget will not, once again, turn into a far more substantial hike. For lessons in restoring fiscal competitiveness and stemming relative economic decline, members of Ontario's provincial parliament could do worse than look east for an example.

References

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