Studies in
Budget & Tax Policy

February 2011

Budget Blueprint

How Lessons from Canada's 1995 Budget Can Be Applied Today

by Niels Veldhuis, Jason Clemens, and Milagros Palacios

Studies in
Budget and Tax Policy

February 2011

Budget Blueprint

How Lessons from Canada's 1995 Budget Can Be Applied Today

by Niels Veldhuis, Jason Clemens, and Milagros Palacios

Contents

Summary / iv

Introduction / 1

1 Where we are today / 2

2 Déjà vu—we've been here before / 11

3 Understanding the successes of the 1990s / 19

4 Applying the lessons of the 1990s today / 30

Conclusion / 47

References / 50

About the authors & Acknowledgments / 57

Publishing information / 59

Supporting the Fraser Institute / 60

About the Fraser Institute / 61

Editorial Advisory Board / 62

Abstract

Canada's federal government has laid out a plan to eliminate its deficit over the next five years. Unfortunately, the current federal plan is based on assumptions of strong revenue growth (based on a strong economic recovery), restrained spending growth, and limited increases in interest rates. Rather than relying on these questionable assumptions about the future, the federal government should have looked at its own experience in the mid-1990s when Canada led the world in solving its deficit and debt problems.

In 1995, the federal Liberal Party undertook deliberate and difficult steps—cutting nominal spending and public-sector employment—and were able to solve the deficit and debt problems of the country effectively. They avoided the mistakes of the preceding decade and a half and took real action. In a short time, their approach brought balanced budgets, declining debt, and decreasing interest costs.

This study is intended to educate readers about the state of the current fiscal problems of the federal government, the parallels with the failures of the 1980s and early 1990s, how governments solved the problems in the mid-1990s, and how we can again solve today's problem using those lessons.

Introduction

Those who cannot remember the past are condemned to repeat it.
George Santayana (1905/1980)

Like most developed countries, Canada is slowly emerging from the financial crisis and ensuing global recession that began in 2007. Like most countries, Canada is struggling to rein in sizeable deficits and avoid debt crises while not jeopardizing economic recovery. Canada's federal government and many of the provincial governments have laid out plans to eliminate their deficits over the coming years. Unfortunately, these plans assume that, over the next number of years, there will be strong revenue growth (based on a strong economic recovery), restrained spending growth, and limited increases in interest rates. Rather than relying on these questionable assumptions, the federal and provincial governments should have looked at their own experiences in the mid-1990s when Canada led the world in solving its deficit and debt problems.

The principal aim of this study is to describe the state of the current fiscal problems at the federal level, the parallels with the failures of the 1980s and early 1990s, how governments solved these problems in the mid-1990s, and how we can solve current problems using those lessons. In many ways, this study is about the virtuous cycle that occurs when governments act promptly and deliberately to eliminate deficits, which leads to surpluses and reduced debt, which allow interest costs to decline, leading to yet more surpluses and less debt, and so on. The study also describes the vicious cycle that can emerge—and emerge quickly—when deficits are not dealt with: accumulating debt, which necessitates increased interest costs, which lead to yet larger deficits, and so on.

The first section of the study examines the federal government's current fiscal plans, its risks, the government's expectations for the future, and the plan to eliminate the deficit. The second section explains how the current circumstances mirror those of the 1980s and early 1990s. The parallels between these two periods are important since they help us understand what works and what does not. The third section describes the historical reforms adopted by the federal government in the mid-1990s. These reforms resulted in balanced budgets, reduced debt, declining interest costs, and a generally prosperous economy. The fourth section outlines a series of reforms based on the successful policies of the 1990s that are designed to return the country to fiscal balance and prosperity.

1 Where we are today

Canada has not been spared the costs and pain of the recent financial crisis and global recession. Like every other industrialized country, Canada has experienced slow or even negative economic growth, increasing unemployment, and deficits. This section summarizes the current financial state of the federal government. It also presents the expectations for the future based on recent government budgets.[1]

Surpluses and deficits

Perhaps the most illustrative measure of the change in Canada's finances is the marked move from consistent surpluses to deficits. Deficits and surpluses indicate the financial performance of the government in any single period, normally a fiscal year. A deficit occurs when the amount of resources collected by the government in the form of taxes and fees is less than the amount spent on direct programs, transfers, and debt charges.

Figure 1 depicts the surpluses and deficits of the federal government as a percentage of the economy (GDP) starting in 1997/98, the first year in which the federal government recorded a surplus after the reforms of the mid-1990s. It also includes the latest expectations of the government over the next five years (2011/12–2015/16).[2] The federal government had a surplus in each year between 1997/98 and 2007/08 and Canada was a world-leader during this period for its ability to balance its financial affairs. Indeed, no other OECD nation (a group of 30 industrial countries)[3] managed to match or better Canada's performance over this period of time (*The Economist*, 2003, September 25).

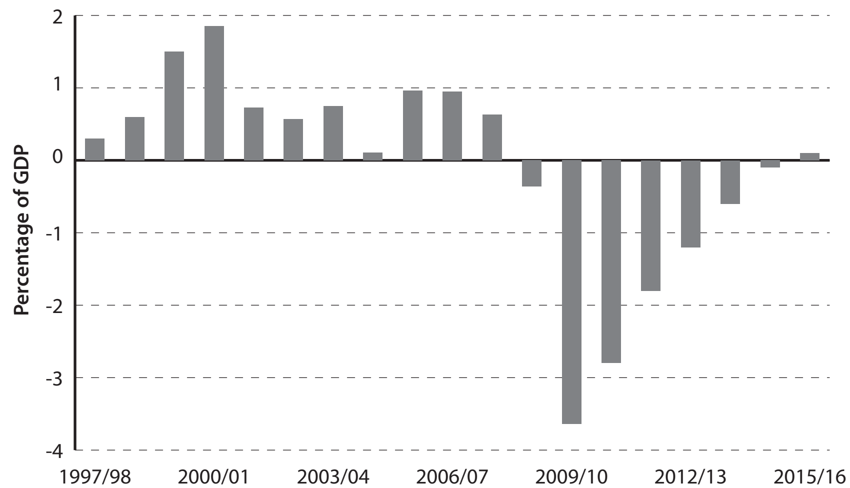
As the global recession took hold in 2008, Canada had a small deficit of $5.8 billion, 0.36% of GDP. This relatively small deficit in 2008/09 was largely due to revenues that were lower than expected revenues: $5.5 billion lower in 2008/09 than originally budgeted in the previous year (Canada, Department of Finance, 2009). The deficit for 2009/10 reached $55.6 billion, 3.6% of GDP. Almost one dollar in four spent on programs by the federal government

1 The principal source of information for the federal government's expectations for the future is *Update of Economic and Fiscal Projections, October 2010* (Canada, Department of Finance, 2010d).

2 The federal government has an operating year that begins on April 1 and ends on March 30. The fiscal years for the federal government are therefore always stated as "2011/12." The provinces also operate on a split calendar year.

3 For information on the OECD, see <http://www.oecd.org>.

Figure 1: Federal deficit or surplus as a percentage of GDP, 1997/98–2015/16



Note: Data for 2010/11 to 2015/16 are based on the federal government's most recent forecast and projections for the future.
Sources: Canada, Department of Finance, 2010c, 2010d.

in 2009/10 was borrowed. This historically high deficit (in terms of dollar values) was caused by a combination of lower revenues and much higher spending than originally planned. Budget revenues for 2009/10 totaled $218.6 billion, lower than the originally expected $224.9 billion and much lower than the previous year's revenues of $233.1 billion (Canada, Department of Finance, 2009; Canada, Department of Finance, Canada, 2010d). The bulk of the deficit, however, is explained by a steep increase in federal program spending to $244.8 billion in 2009/10 from $207.9 billion the previous year, an increase of 17.7% (see figure 4 for more details). This level of spending was also well above the $229.1 billion planned originally in the 2009 Budget.

The federal government does not expect to return to a balanced budget or surplus until 2015/16 (figure 1). The expected surplus in 2015/16 is $2.6 billion, 0.10% of GDP or 0.85% of expected budget revenues, a surplus in name only. In the meantime, between 2008/09, when it first began running a deficit, and 2015/16, the federal government expects to incur over $171.0 billion in debt.

Recall that a deficit refers to a period in which a government spends more than it collects in revenues. The result of deficits is debt, which is simply the accumulation of deficits over time.[4] It is not surprising, given the

4 Debt can also be incurred when long-term financing, such as bonds, are issued to pay for long-term assets. For example, a government might determine that the building of a highway or bridge is in the long-term interest of its citizens. It issues long-term bonds to raise the resources needed to build the infrastructure and then subsequently pays back the bonds over time as the benefits from the infrastructure accrue.

results shown in figure 1, Canada's national debt[5] is expected to increase over the next four years. Figure 2 shows the dollar value of Canada's federal debt from 2000/01 to that expected in 2015/16. The marked increase in Canada's federal debt beginning in 2008/09 when deficits reappeared is unmistakable. Canada's debt has increased from a low of $457.6 billion in 2007/08 to nearly $519.1 billion in 2009/10. It is expected to reach a high of $628.7 billion by 2014/15 before starting to decline when the country again has budget surpluses. It is not an exaggeration to say that Canada's national debt has ballooned over the last two years and will continue to do so until leveling off in 2012/13.[6]

The increase in the country's federal debt is less dramatic when compared to the size of the economy. Debt as a share of GDP is an important measure since recent research has demonstrated the serious costs imposed on economies in the form of slower economic growth and the risks of financial crises when government debt reaches certain thresholds (Reinhart and Rogoff, 2009; International Monetary Fund, 2008). Federal debt as a share of the economy (GDP) reached a low of 29.0% in 2008/09. It is expected to increase to 35.3% in 2011/12 before starting to decline with renewed economic growth. Recall that the dollar value of the federal debt will continue to increase until 2015/16.

Higher interest charges

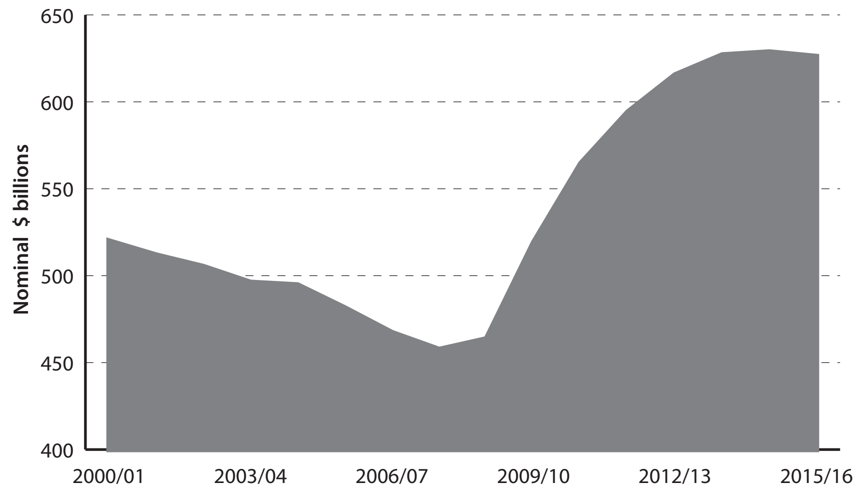
One of the costs of deficits and the related increase in debt is higher interest charges, the interest payments made on the stock of existing debt. They do not include payments that reduce the amount of outstanding debt. Interest charges on the country's federal debt are expected to increase over the next five years. As shown in figure 3, federal interest charges hit a low of $29.4 billion in 2009/10. They have since increased, and are expected to reach $37.8 billion in 2014/15, an increase of 28.6%. Indeed, the latest projections by the federal government indicate that interest costs will continue to increase over the government's budgeting period (figure 3).

It's important to understand what is referred to as the wedge effect of interest costs. Interest charges create a wedge between what a government collects in resources (that is, taxes and fees) and what the government actually spends on programs and services. The best measure available to gauge this wedge between revenues and actual spending on programs is to examine interest charges as a share of budget revenues. The federal government's share

5 There are a variety of different measures of debt. For a number of reasons, including consistency, we have chosen to use a series referred to as "accumulated deficits," which measures gross or total debt minus financial and non-financial assets.

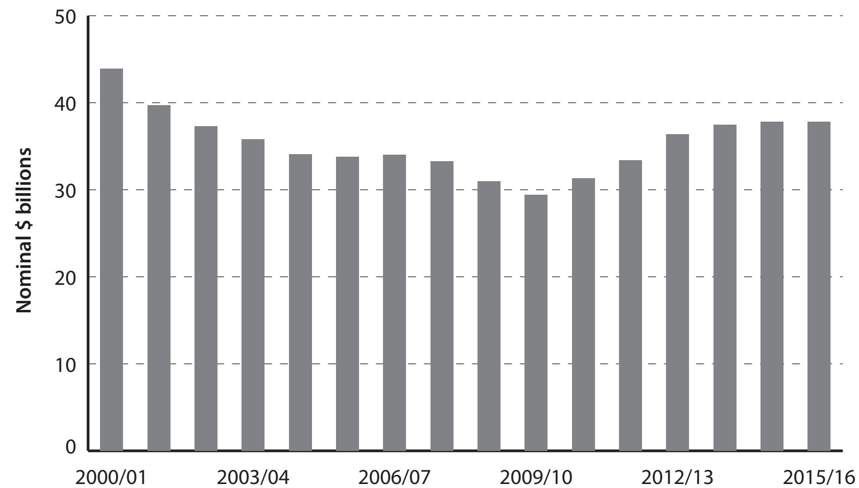
6 Relatively small increases in the dollar value of the national debt are recorded in 2013/14 and 2014/15.

Figure 2: Federal debt (nominal $ billions), 2000/01–2015/16



Notes: Data for 2010/11 to 2015/16 are based on the federal government's most recent forecast and projections for the future. There are several series available for measuring federal debt. The series chosen for this study is accumulated deficits, which measures gross or total debt minus financial and non-financial assets.
Sources: Canada, Department of Finance, 2010d.

Figure 3: Federal interest charges (nominal $ billions), 2000/01–2015/16



Note: Data for 2010/11 to 2015/16 are based on the federal government's most recent forecast and projections for the future.
Sources: Canada, Department of Finance, 2010a, 2010c; 2010d.

of budget revenues dedicated to interest costs steadily declined beginning in the late 1990s, reaching a low of 13.3% in 2008/09, but began to climb again in 2009/10 (figures 22a, 22b, figure 3). They are expected to peak in 2012/13 at a little less than 14.0% of revenues. This upward trend is expected to continue until 2013/14 based on the federal government's current assumptions about GDP and interest rates since, while nominal interest costs are

expected to rise throughout this period (figure 3), the current budget assumes revenues will grow faster than interest costs. However, if the current assumptions about interest rates and GDP growth prove overly optimistic, the wedge between the resources collected and what is available for spending could easily increase.

Spending expectations

Thus far we have outlined the state of the current deficit, the federal government's expectation of again having a surplus in 2015/16, and the implications of deficits on debt and interest costs. To understand the government's plan for a return to surplus, it is important to examine the government's expectations about spending and revenue over the next five years.

Figure 4 illustrates federal spending, both program and total spending, from 2000/01.[7] The figure shows two important facts. One, except during a few years, both program and total spending have been steadily increasing since 2000/01. Indeed, even before the recession hit in 2008/09 program spending had increased from $130.6 billion in 2000/01 to $207.9 billion in 2008/09, an increase of almost 60% in less than a decade. The government expects program spending to reach $265.4 billion in 2015/16, more than double the amount spent in 2000/01. The second important fact is the presence of the stimulus in 2009/10,[8] when program spending increased by $36.9 billion (17.7%). The intent of the federal government was to combat the recession through traditional Keynesian methods, that is, through a combination of increased government spending (purchases) and tax relief designed to stimulate consumer spending.[9]

Note in figure 4 the absence of any meaningful or sustained decline in spending. After 2009/10, there is a decline in the *growth* of program and total spending but no reduction in spending itself except for the small scheduled reduction in 2011/12.[10] Stimulus spending, which is by design meant to be temporary would require a return to normal spending after the money allocated for stimulus is exhausted. However, the spending profile illustrated in figure 4 indicates that the stimulus spending is simply more permanent spending over time rather than a one-time or temporary increase in spending.

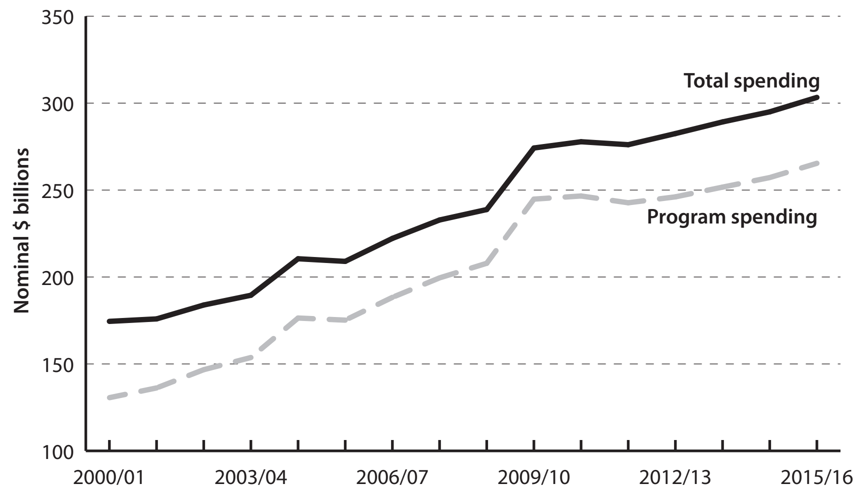
7 It is important to recognize that program spending is at the discretion of the government while total spending is partially driven by factors out of its control. For instance, total spending includes interest charges, whose dollar value is determined by market forces.

8 For information about the federal stimulus plan, see Canada, Department of Finance, 2010b; TD Economics, 2009.

9 For a discussion of the effectiveness of the federal government's stimulus spending, see Karabegović, Lammam, and Veldhuis, 2010.

10 Program spending is scheduled to decline by $3.9 billion (1.6%) and total spending is forecast to decline by $1.7 billion (0.6%) in 2011/12 (Canada, Department of Finance, 2010d).

Figure 4: Federal total and program spending (nominal $ billions), 2000/01–2015/16



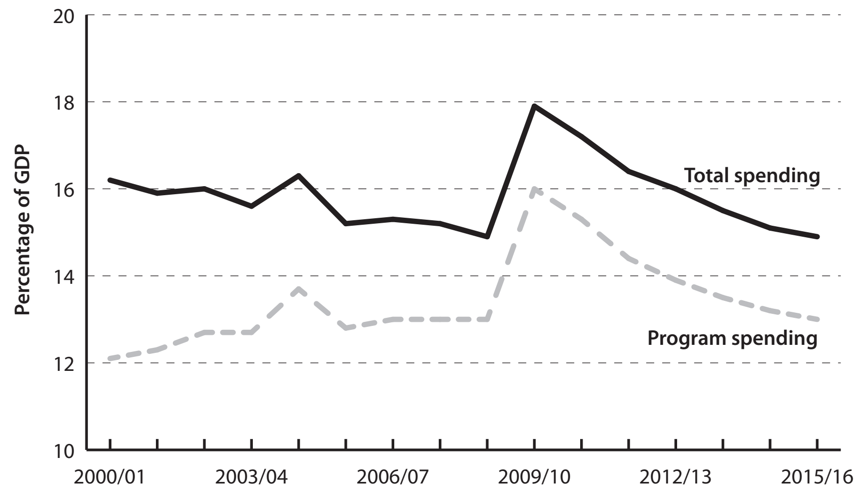
Note: Data for 2010/11 to 2015/16 are based on the federal government's most recent forecast and projections for the future.
Sources: Canada, Department of Finance, 2010a, 2010c, 2010d.

Figure 5 shows federal program and total spending as a percentage of the economy (GDP) and the effect of the 2009/10 stimulus plan is even more evident. Program spending increases from 13.0% of GDP in 2008/09 to 16.0% of GDP in 2009/10. The government expects both total and program spending to decline as a share of the economy over the next five years. However, neither total nor program spending will return to its pre-stimulus share of the economy (14.9% and 13.0%) until 2015/16. Critically, this achievement is not due to reductions in spending: recall that spending, both total and program, does not decline over the next five years (figure 4). Instead, its rate of growth is slowed. The reduction in spending as a share of the economy is entirely a function of reducing the growth in spending coupled with stronger economic growth rather than an actual reduction in nominal spending.

This reliance on stronger GDP growth and the related growth in budget revenues rather than on direct action by the government in the form of spending reductions is the Achilles' heel of the federal government's current plan, as will be shown later in the study. Figure 6 graphically compares the annual growth in program and total spending with the change in population and inflation (CPI) in the same year. The figure illustrates the difference between how much spending actually increased and what was required to accommodate increases in population and prices.

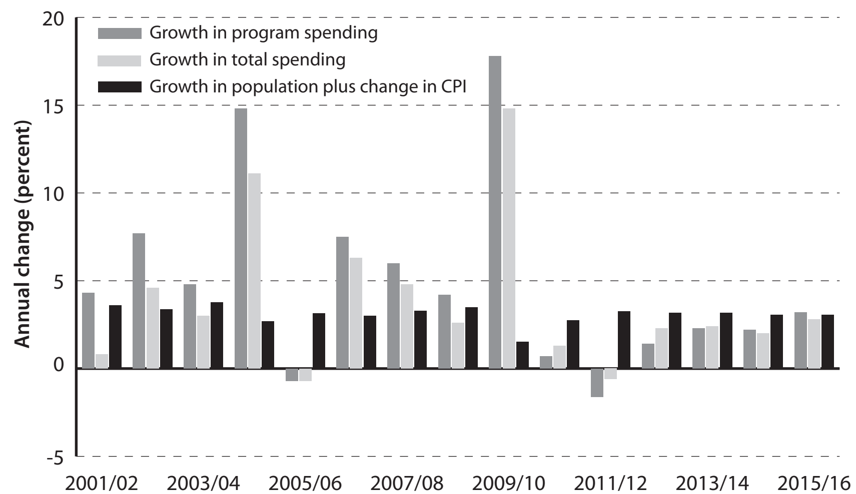
In interpreting figure 6, it is important to break the period from 2000/01 to 2015/16 into two parts: pre-stimulus (before 2009/10) and post-stimulus. Before the federal government enacted the stimulus package of 2009/10, government program spending had increased faster than population

Figure 5: Federal total and program spending (percentage of GDP), 2000/01–2015/16



Note: Data for 2010/11 to 2015/16 are based on the federal government's most recent forecast and projections for the future.
Sources: Canada, Department of Finance, 2010a, 2010c, 2010d.

Figure 6: Growth in federal spending compared to growth in population plus change in the Consumer Price Index (CPI), 2001/02–2015/16



Notes: Population growth was forecast at 10-year average of 1.06% growth rate. Data for 2010/11 to 2015/16 are based on the federal government's most recent forecast and projections for the future.
Sources: Canada, Department of Finance, 2010a, 2010c, 2010d; Statistics Canada 2010a, 2010c; calculations by the authors.

growth and increases in prices every year except 2005/06: in seven of the eight years between 2001/02 and the stimulus of 2009/10, government program spending increased faster than population and inflation.[11] The growth in total spending was less marked: total spending increased faster than population growth and inflation in four of the years during this period. Recall that the difference between total spending and program spending is debt charges.

Fiscal year 2009/10 clearly shows a marked increase in spending based on the stimulus program. The government's plan is for program as well as total spending to increase at a rate lower than population growth and inflation in every year between 2010/11 and 2014/15 (figure 6). However, only in 2011/12 are both program and total spending expected to decline in terms of dollar value; and only by marginal amounts (1.6% and 0.6%). The key to the federal government's plan is slowing the *growth* in the increases in spending over the next five years. This can be seen in the latter part of figure 6 where growth in spending is constrained. A major risk to this plan is obvious: if spending growth is not sufficiently constrained, the government will fail to reach its fiscal objectives. There are numerous scenarios—for example, an election call—where it would be prohibitively difficult for the government to constrain growth in spending.

Revenue expectations

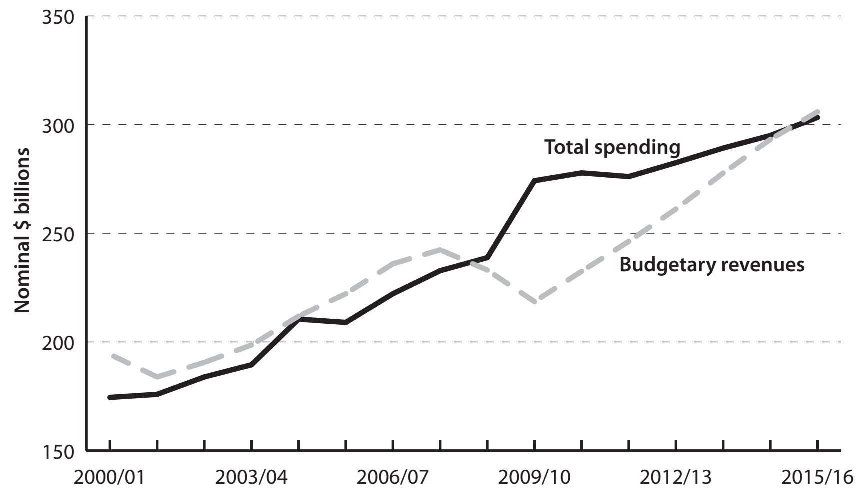
The key objective the federal government has set out is returning to a balanced budget or a surplus by 2015/16. Figure 7 illustrates the achievement of that objective by comparing budget revenues and total spending, both actual to-date and planned in the future. The achievement of a balanced budget in 2015/16 is the result of two principle factors. The first, discussed above, is a slowdown in the growth of spending by the federal government. This can be seen in the flattening of the spending line in figure 7 after 2009/10. The second contributing factor is the projected rebound of budget revenues beginning in 2010/11. The steep recovery in budget revenues based on strong economic growth allows the federal government to achieve a balanced budget in five years while still increasing spending over that time period. Clearly, there is a second major risk to the federal government's plan: it relies on a strong rebound in the growth of GDP and budget revenues that may not materialize.[12]

---

11 For a discussion of the relationship between government spending and economic performance, see Alesina, Ardagna, Perotti, and Schiantarelli, 2002; and Alesina, Perotti, Giavazzi and Kollintzas, 1995.

12 Interestingly, table 2.1 in the *Update of Economic and Financial Projections, October 2010* (Canada, Department of Finance, 2010d) shows downward revisions for both nominal and real GDP in 2011, 2012, and 2013. The estimates for 2013 and 2014 showed a mix of stable and moderately increasing revenue.

Figure 7: Federal revenues and spending (nominal $ billions), 2000/01–2015/16



Note: Data for 2010/11 to 2015/16 are based on the federal government's most recent forecast and projections for the future.
Sources: Canada, Department of Finance, 2010a, 2010c, 2010d.

Conclusion

The federal government now has sizeable budget deficits, which are leading to the accumulation of debt and increasing interest costs. The current deficit is a function of reduced revenues and, to a much greater extent, higher spending. Indeed, spending increases by the federal government had been sizeable for many years even before the crisis of 2008. More importantly, the one-time, temporary stimulus spending seems to have been folded into future permanent spending and the federal government's plans do not show spending returning to its pre-stimulus levels, even after adjusting for growth in the population and increases in prices.

The government's plan to return to a balanced budget calls for a slower rate of growth in federal spending over the next five years that will allow revenues to catch up as the economy recovers. The government assumes it can restrain spending growth for the next five years while strong economic growth brings higher revenues. The risks of such an approach are clear: failure to slow increases in spending, lower than expected growth in GDP and revenues, or interest costs higher than expected could all derail the government's plan and leave the federal government with an ongoing deficit.

2 Déjà vu—we've been here before

The federal government's current plan to reduce the deficit appears to ignore its own recent history. Canada faced an even more serious fiscal situation for the better part of a decade-and-a-half before real fiscal reforms were enacted in 1995. The reforms of 1995, however, were materially different from the plan that has been laid out by the current federal government. Indeed, part of the inability of the federal government to reduce the deficit in the 1980s and early 1990s was that it relied on a plan similar to the one being used now. This section describes the problems faced by the federal government throughout the 1980s and early 1990s and how successive governments failed to solve these problems.

Deficit and debt from 1980/81 to 1995/96

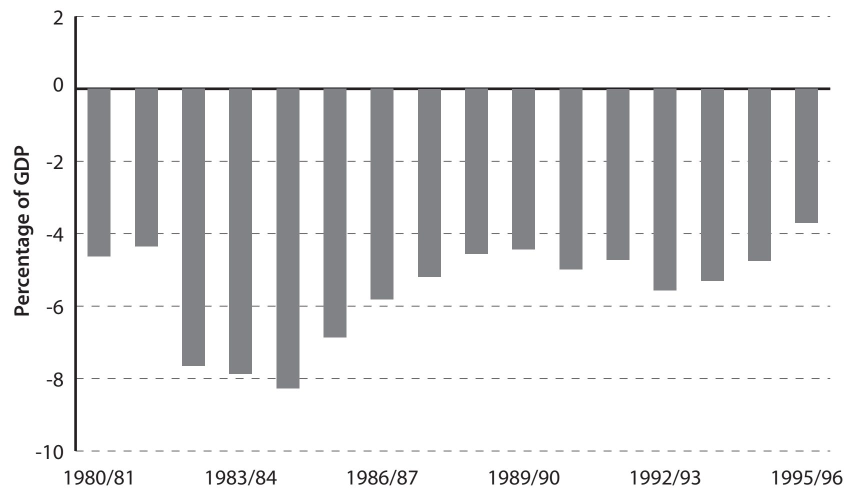
Figure 8 shows the federal government's deficit as a share of the economy (GDP) from 1980/81 to 1995/96 the year of the fiscal reform. There was no year in this period in which the federal government had a surplus and the deficit ranged from a low of $14.6 billion in 1980/81 to a high of $39.0 billion in 1992/93.[13] As a share of the economy, the federal deficit ranged from a low of 4.4% of GDP in 1981/82 to a high of 8.3% of GDP in 1984/85. The deficit in 2009/10 was 3.6% of GDP so, although the dollar value of the deficit in 2009/10 was substantially greater than the highest level of the 1980s and early 1990s, as a share of the economy it is much smaller, which should allow the government to eliminate the deficit more easily than it did in the mid-1990s.

Given the enormous deficit of the federal government from 1980/81 to 1995/96, it should come as no surprise that there was a marked increase in the federal debt: the federal debt increased from $227.8 billion in 1985/86 to $554.2 billion in 1995/96 (Canada, Department of Finance, 2010c). Figure 9 presents the value of the federal debt as a share of GDP from 1985/86 to 1995/96.[14] Federal debt as a share of the economy increased from 46.9% in 1985/86, worrying enough, to 68.4% in 1995/96. Indeed, the increase in the federal debt over this time period is almost a straight line without any interruption.

13 For reference purposes, the dollar value of the deficit in 2009/10 was $55.6 billion (Canada, Department of Finance, 2010d).

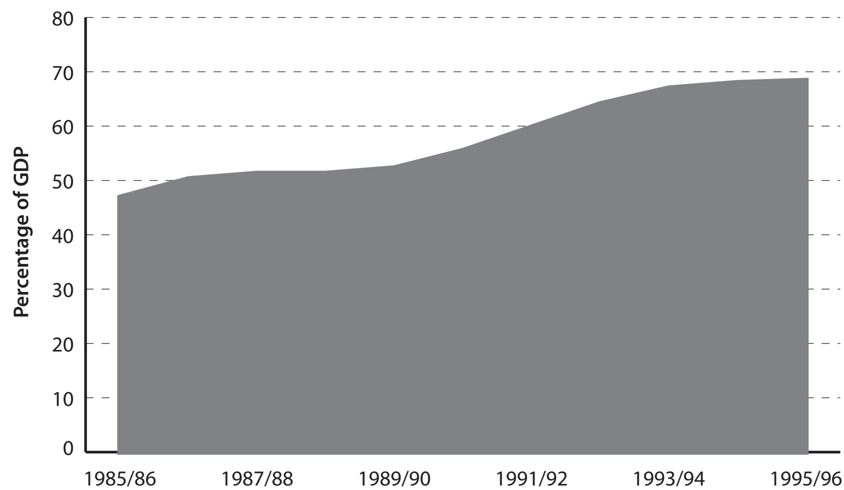
14 The series used for debt is not available on a consistent basis before 1983/84 due to a change in accounting.

Figure 8: Federal deficit (percentage of GDP), 1980/81–1995/96



Source: Canada, Department of Finance, 2010c.

Figure 9: Federal debt (percentage of GDP), 1985/86–1995/96



Notes: Data for 2010/11 to 2015/16 are based on the federal government's most recent forecast and projections for the future. There are several series available for measuring federal debt. The series chosen for this study is accumulated deficits, which measures gross or total debt minus financial and non-financial assets.
Source: Canada, Department of Finance, 2010c: tables 1 and 2.

It is important to understand this increase in federal debt to 68.4% of GDP in 1995/96 in the light of emerging research about the economic effects of government debt.[15] Recent research by Carmen M. Reinhart of the University of Maryland and Kenneth S. Rogoff of Harvard University on the economics of debt accumulation by government indicates a threshold of

15 See Reinhart and Rogoff, 2009 and International Monetary Fund, 2008 for recent research on the economics of debt accumulation by government.

debt accumulation of 90% of GDP after which economies tend to experience slower economic growth and related costs (Reinhart and Rogoff, 2009). This threshold is important because in 1995/96 the federal government's debt-to-GDP ratio of 68.4% combined with the consolidated provincial debt-to-GDP ratio of 27.6% meant that Canada had exceeded the threshold identified by Reinhart and Rogoff, even before municipal and other government debt was included.[16]

As the national debt expanded, so too did the costs of maintaining the debt: interest costs. In fact, the situation was made worse since interest rates themselves were generally increasing for much of the decade. The nominal interest costs faced by the federal government increased from $10.7 billion in 1980/81 to $45.0 billion in 1990/91 before decreasing slightly as interest rates declined. They increased again, however, in 1994/95 as international capital markets began to re-assess the riskiness of Canadian government debt (figure 10a). For comparative purposes, nominal interest costs in 2009/10 were $29.4 billion and rising.

Recall that interest costs create a wedge between the resources collected by government as taxes and fees and the amount of those resources the government is able to spend on programs and services. The share of revenues spent on interest costs increased from an already worrying 20.0% in 1980/81 to 37.6% in 1990/91. Even after the slight declines observed in the early 1990s, interest costs still generally consumed more than one-third of revenues up to 1995/96 (figure 10b). The enormity of the problems associated with having one-third of resources collected allocated to interest costs cannot be overemphasized. Indeed, this is one of the key factors prompting the historic reforms enacted in 1995.

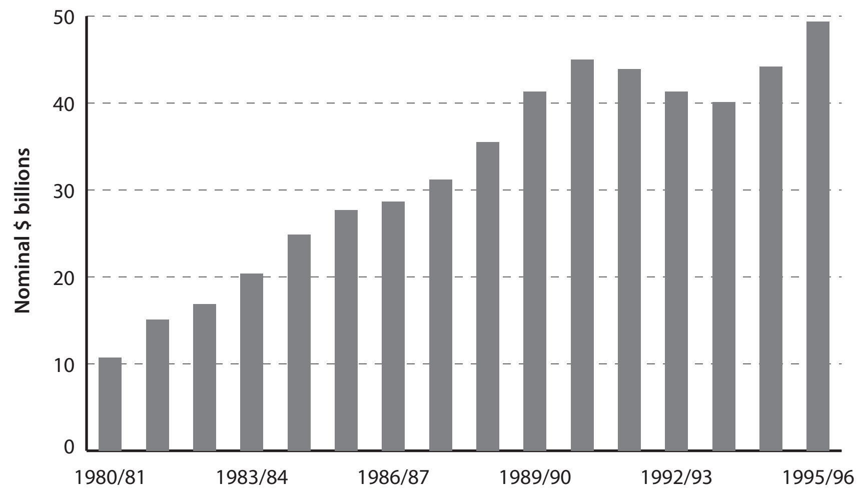
Interest charges, spending, and revenue from 1980/81 to 1995/96

One of the benefits of the reforms in the 1990s has been that, even when the federal government again incurred a deficit, interest costs as a share of revenues have remained well below the levels of the 1990s. In 2009/10, for instance, interest costs consumed only 13.5% of budget revenues (figure 3). This affords the current federal government more latitude than was the case in the 1980s and 1990s. However, that flexibility should be used to solve the problem more quickly rather than taking the slower approach the federal government has chosen.

---

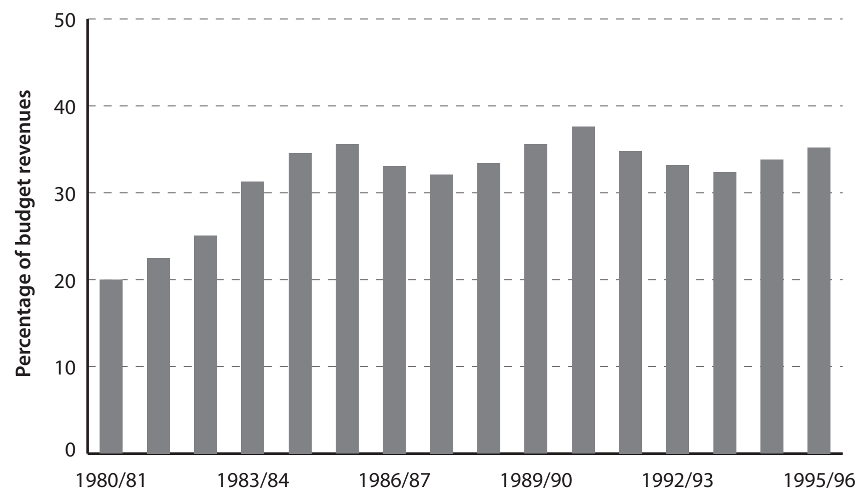
16 On a national accounts basis, the total liabilities of the federal, provincial, and local governments as of 2009 totaled $1,643 billion, which was composed of $775.1 billion in federal liabilities and $864.9 billion in provincial and local liabilities (Canada, Department of Finance, 2010c: tables 48, 49, and 51). In addition, we recommend the Fraser Institute's cataloging study of government liabilities and its discussion of government enterprise (GBE) debt and other indirect liabilities such as debt guarantees (Palacios, Veldhuis, and Harischandra, 2008).

Figure 10a: Federal interest charges (nominal $ billions), 1980/81–1995/96



Source: Canada, Department of Finance, 2010c.

Figure 10b: Federal interest charges (percentage of budget revenues), 1980/81–1995/96

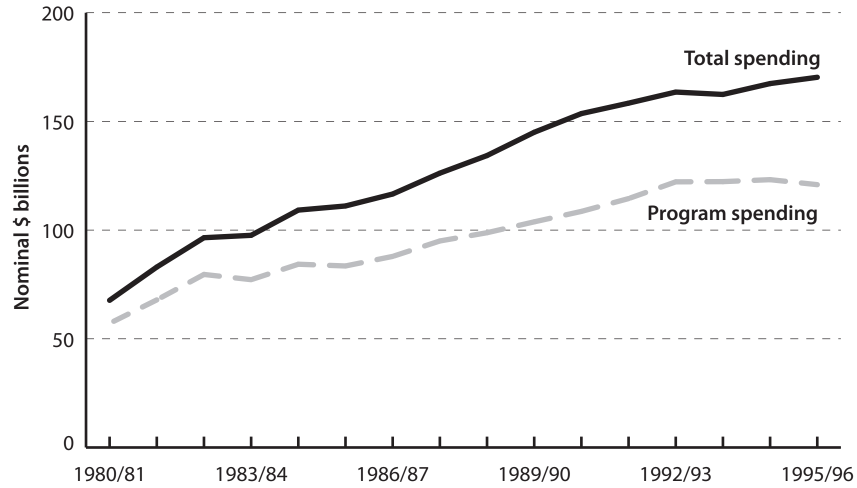


Source: Canada, Department of Finance, 2010c; calculations by authors.

Figure 11 shows total and program spending by the federal government from 1980/81 to 1995/96. What is abundantly clear is that, even though the federal government was facing constant deficits, accumulating debt, and alarming interest costs, both program and total spending continued to increase throughout this period save for 1993/94, in which there was a small decrease in program spending.[17] Figure 12 compares the annual rates

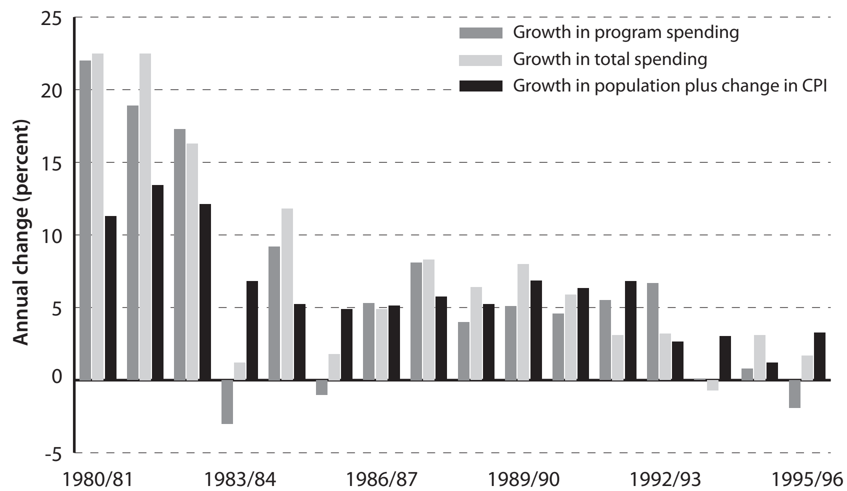
17 Total spending fell by $1.1 billion in 1993/94, representing a decline of 0.7% (Canada, Department of Finance, 2010c).

Figure 11: Federal total and program spending (nominal $ billions), 1980/81–1995/96



Source: Canada, Department of Finance, 2010c.

Figure 12: Growth in federal spending compared to growth in population plus change in the Consumer Price Index (CPI), 1980/81–1995/96



Sources: Canada, Department of Finance, 2010c; Statistics Canada, 2010a, 2010c; calculations by authors.

of growth in both total and program spending by the federal government with the increase in population and changes in prices from 1980/81 to 1995/96. The period can be divided into two parts. The first, from 1980/81 to about 1984/85, was characterized by fairly high rates of inflation. In only one year did the growth in program spending not exceed the rate of population growth and inflation. Indeed, in many years the gap between the increases in spending and the rate of population growth and inflation were substantial. For example, the growth in both total and program spending in 1980/81 was almost double the rate of population growth and inflation.

The second part of the period from 1980/81 to 1995/96 begins in 1985/86 and was characterized by lower rates of inflation. The growth in both total and program spending during this period was much closer to the rates of population growth and inflation. There were also many years in which spending growth was constrained during this period though this was not done consistently.

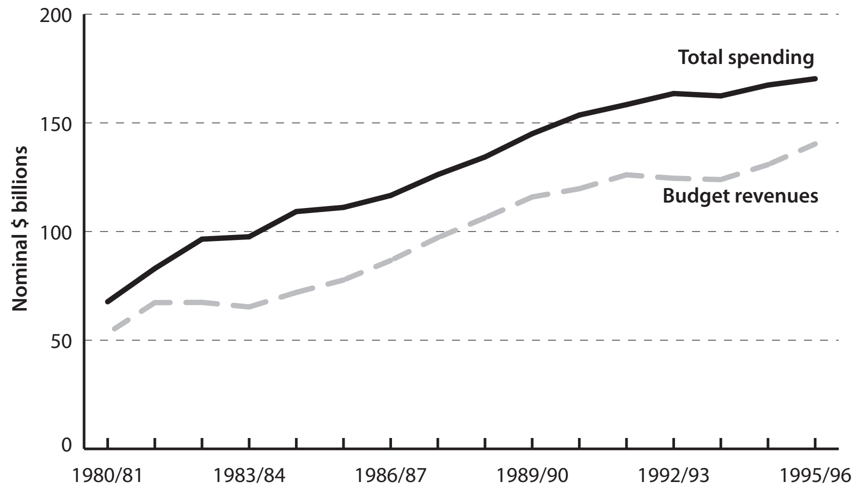
As discussed above, this period was characterized by sizeable deficits. Figure 13 shows the same data as figure 8 except that it dissects it into revenues and spending, the balance of which results in deficits or surpluses. Throughout this period, budget revenues grew but that the growth was insufficient to catch up with the annual growth in spending. Indeed, the gap—the size of the deficit—increased over this time period. So the question remains, then, why the federal government could not make greater progress in closing the deficit gap during this period. The question is even more perplexing considering that that the government of the day (Progressive Conservative Party) was at least notionally predisposed to lower levels of government spending and balanced budgets.

Part of the answer to this question is found in increasing interest rates and consequent increasing interest costs. However, this overlooks a critically important part of the explanation for the government's failure to deal effectively with the deficit. Put simply, the plan used by the government to address the deficit was flawed: rather than reducing spending in any meaningful way, the government tried to slow the growth in spending while hoping for strong growth in revenue, exactly the same approach relied upon today by the current federal government.

Figure 14 shows the federal government's expectations of revenue in each of the budgets between 1984 and 1987. In four budget periods, there were two fairly marked reductions in the revenues expected and it is clear that the federal government twice had to lower its expectations of what it would collect in budget revenues over this four-year budget period. For example, between the 1984 and 1985 budgets, the federal government reduced its four-year revenue forecast by $11.5 billion. In other words, in its 1985 budget the federal government expected to collect $11.5 billion less over the four-year period from 1983/84 to 1986/87 than it had in the previous 1984 budget. A similar, though smaller, reduction in forecast revenue occurred between the 1986 and 1987 budgets.

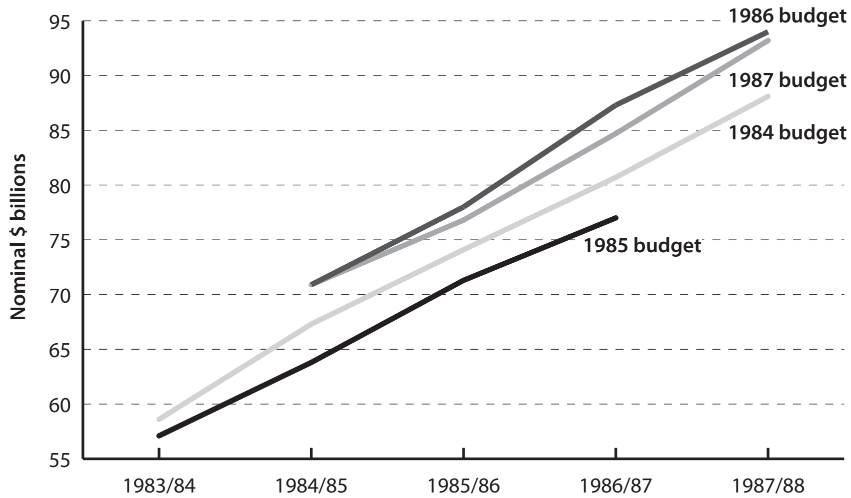
Interestingly, even as revenues did rebound and revenue expectations increased, the federal government was still unable to move closer to a balanced budget. The main reason for this failure is captured by the undeniable trend in figure 15, which shows the revised government estimates for total spending based on successive budgets from 1983 through to 1989. In each successive budget, the expectation for total spending in each fiscal year is always either stable or increased. Clearly, the federal government had tremendous difficulty in constraining growth in spending and, even as revenues grew, they were not able to catch up with the higher level of spending, which resulted in ongoing deficits.

Figure 13: Federal revenues and spending (nominal $ billions), 1980/81–1995/96



Source: Canada, Department of Finance, 2010c.

Figure 14: Revised estimates for federal budget revenues (nominal $ billions), 1984–1987 Budgets

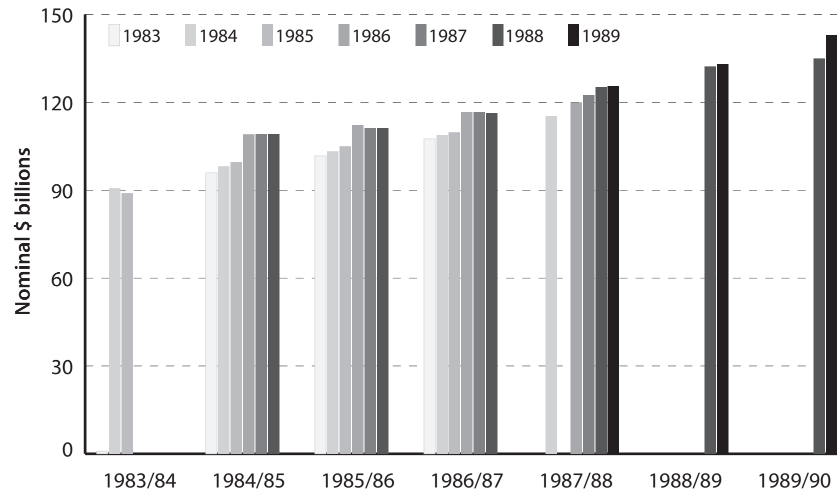


Sources: Canada, Department of Finance, 1984, 1985, 1986, 1987.

Conclusion

The parallels between the situations faced today and in the period from 1980/81 to 1995/96 are striking. In both periods, the federal government faced deficits and increasing debt coupled with increasing interest costs and the pressures those increases impose on government. Indeed, the pressures faced by the federal government in the 1980s and early 1990s were greater than is currently the case.

Figure 15: Revised estimates for federal total spending (nominal $ billions), 1983/84–1989/90 Budgets



Sources: Canada, Department of Finance, 1984, 1985, 1986, 1987.

Perhaps most importantly, both governments tried to reduce the deficit, not by reducing spending, but by constraining growth in spending while waiting for the stronger revenue growth it assumed would come. The failure of the government's plan in the 1980s and early 1990s came from its inability to constrain growth in spending coupled with revenues lower than expected. The failure of the government to solve its fiscal problems meant ongoing deficits, mounting debt, and increasing interest costs.

3 Understanding the successes of the 1990s

Jean Chrétien's Liberal Party was swept into office in 1993.[18] Their first budget (1994) is generally considered a status quo budget and one that did not undertake the difficult steps needed to rein in the deficit (Richards, 2000).[19] The financial situation the government faced in fiscal year 1994/95 was daunting: the deficit had reached $36.6 billion, 4.75% of GDP, and the debt had reached $524.2 billion, 68.0% of GDP. Interest costs paid by the government on the national debt reached $44.2 billion, consuming 33.8% of budget revenues.

The deteriorating finances of the government coupled with a number of other factors motivated—some argue, forced—the government to act. It is worth highlighting the other factors to clarify the circumstances within which this historic fiscal reform occurred. Politically, the unified, ideologically coherent, opposition of Preston Manning's Reform Party was instrumental in establishing a parliamentary environment receptive to, and supportive of, many of the fiscal reforms proposed and enacted by the governing Liberals. In addition, a broad array of think tanks, advocacy groups, and business organizations had been educating the public on the risks and costs of the deficit and debt, such that the general public increasingly supported change. Reforms implemented in Saskatchewan by Roy Romanow's NDP government and in Alberta by Ralph Klein's Conservatives created some political consensus regarding the need and efficacy of change.[20]

Externally, the collapse of the Mexican Peso in 1994 provided real world evidence of the costs of ignoring deficits and debt. An editorial in the *Wall Street Journal* that commented on Canada's debt problem and suggested the country was nearing bankruptcy caused a sharp decline in the value of the Canadian dollar (*Wall Street Journal*, 1995, Jan. 12).[21] Interest rates were rising throughout the year and there was increasing concern about

18 For elections results, see <http://www2.parl.gc.ca/Sites/LOP/HFER/hfer.asp?Language=E&Search=G>.

19 While the 1994 Budget did not include measures to tackle the deficit, it did include a commitment to "review" every government agency and program over the course of 1994 with an eye to ensuring appropriate "size, scope, composition and cost" (Martin, 1994: 13). This broad review would turn out to be critical for the subsequent 1995 Budget.

20 For a more thorough discussion of the reforms implemented in Saskatchewan and Alberta as well as in Ontario, see Crowley, Clemens, and Veldhuis, 2010.

21 David Dodge, then associate deputy minister of finance and later Governor of the Bank of Canada, called the *Wall Street Journal*'s article a "seminal event" (cited in Savoie, 1999: 178).

Canada's fiscal situation. International organizations such as the International Monetary Fund and the Organisation for Economic Co-operation and Development (OECD) were calling for faster reductions in the country's deficit (Beauchesne, 1994, Dec. 6). These and other factors culminated in the delivery of the Liberal Party's 1995 budget, which is one of the most important budgets in modern Canadian history.

1995 Budget—announcing and implementing historic reforms

The 1995 Budget set in motion fundamental fiscal reforms and ultimately became a defining moment in Canada's fiscal history. In his budget speech, Finance Minister Paul Martin boldly articulated a new direction for the government: "We are acting on a new vision of the role of government … smaller government … smarter government" and put the issue of the deficit in non-partisan terms when he stated that "[t]he debt and deficit are not inventions of ideology. They are facts of arithmetic. The quicksand of compound interest is real" (Martin, 1995: 2).

Table 1 summarizes the fiscal plan proposed by the government in the 1995 Budget. Unlike the previous attempts to tackle the deficit—and the approach of the current government—the governing Liberal Party planned to reduce nominal spending: the plan called for a reduction of program spending from $118.3 billion in 1994/95 to $107.9 billion in 1996/97 (table 1). The government proposed cutting program spending by $10.4 billion, representing a decline of 8.8% over a two-year period. The budget also reduced public sector employment by 45,000 or 14%. As illustrated in figure 16,[22] the government not only achieved its plan but exceeded it. Over two years (1995/96 and 1996/97), the federal government reduced program spending by $11.9 billion, a cut of of 9.7% (figure 16). Again, this was not a slowing of growth in spending over time but rather a reduction in the amount of spending. Importantly, the government also constrained growth in spending after 1997/98 for three additional years.

Figure 17 compares the growth in total and program spending with the rate of growth in population and inflation. What is evident from figure 17 is that the federal government not only cut spending in 1995/96 and 1996/97 but also continued to constrain the growth of spending compared to population growth and inflation through to 1999/00. Beginning in 2000/01 and throughout the remainder of the years covered in figure 17, the federal government allowed spending, particularly program spending, to grow at rates well in excess of the growth of the population and inflation. However, the lessons for this study are to be found in the great achievements of 1995/96 to 1999/00.

---

22 Please note that the figures included in table 1 reflect budgeted or planned spending rather than the actual spending shown included in figure 16.

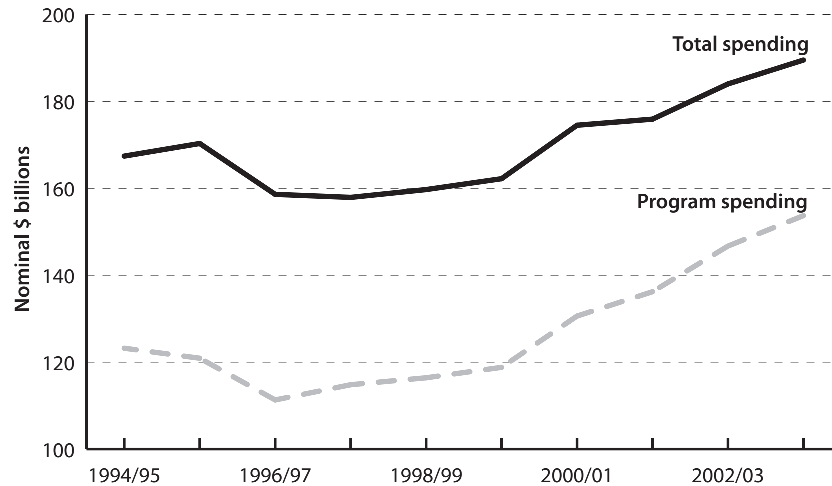
Table 1: Fiscal Outlook presented in the 1995 Federal Budget

	1994/95	1995/96	1996/97
	$ billions		
Revenue	125.0	133.2	137.4
Program Spending	118.3	114.0	107.9
Debt Charges	42.0	49.5	50.7
Total Spending	160.3	163.5	158.6
Deficit	37.9	32.7	24.3
	Percent of GDP		
Revenue	16.7	16.9	16.7
Program Spending	16.2	14.5	13.1
Deficit	5.1	4.2	3.0

Notes: Numbers may not add due to rounding or the exclusion of other relatively minor line items. Data for 1994/95 are preliminary estimates. 1995/96 and 1996/97 are forecasts.

Source: Canada, Department of Finance, 1995b.

Figure 16: Federal total and program spending (nominal $ billions), 1994/95–2003/04

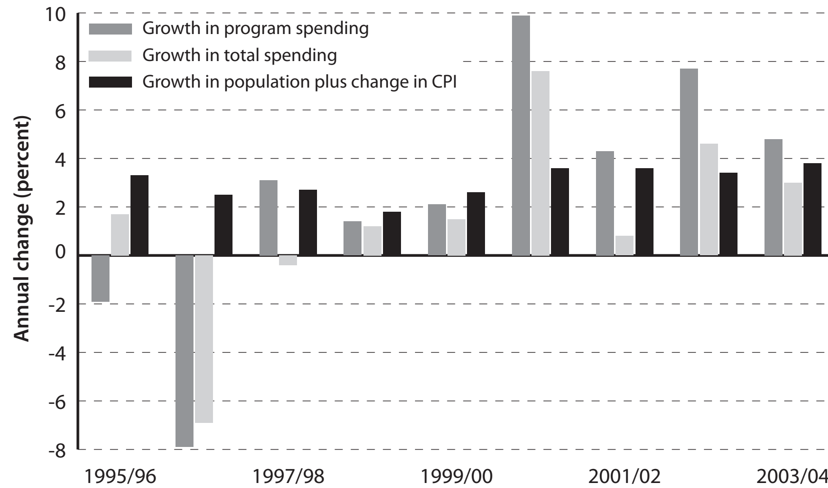


Source: Canada, Department of Finance, 2010c.

A critical aspect of the reductions in spending was the concurrent reduction in the size of government compared to the economy.[23] Figure 18 illustrates the decline in federal total and program spending as a share of GDP the economy over this period: program spending decreased from 16.0% of GDP in 1994/95 to a low of 12.1% of GDP by 2000/01 (figure 18).

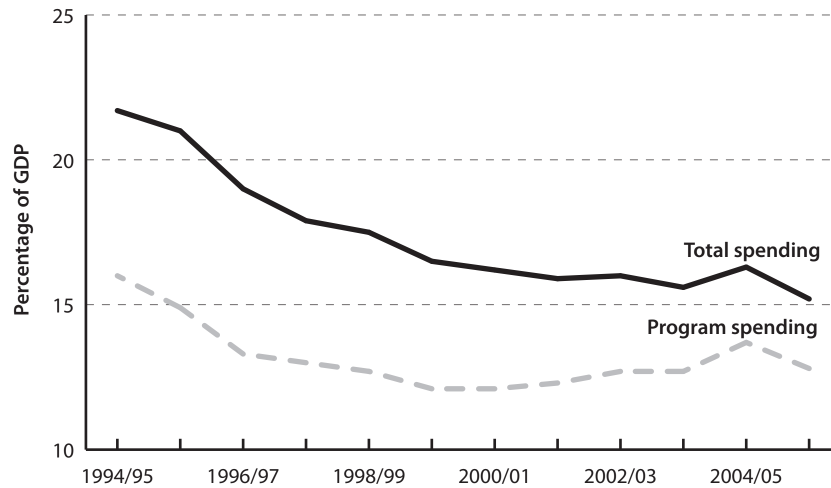
23 For a recent summary of the research on the economics of the size of government, see Clemens, Veldhuis, and Kaszton, 2010: 15–22.

Figure 17: Growth in federal spending compared to growth in population plus change in the Consumer Price Index (CPI), 1995/96–2003/04



Sources: Canada, Department of Finance, 2010c; Statistics Canada, 2010a, 2010c; calculations by authors.

Figure 18: Federal total and program spending (percentage of GDP), 1994/95–2005/06



Source: Canada, Department of Finance, 2010c.

It then increased slightly from the low attained in 2000/01 to 13.7% in 2004/05. Total spending decreased from 21.7% of GDP in 1994/95 to 15.2% of GDP in 2005/06.

Getting government right—program review

Unlike other governments, which have tackled deficits by cutting spending across the board, the Canadian federal government during the latter half of the 1990s relied on a methodical approach that avoided deep cuts to important areas while areas of lower priority carried a greater burden for

the reduction in spending. In other words, the Finance Minister's "smaller … smarter government" (Martin, 1995). This process of setting priorities was called the Program Review, a comprehensive examination of federal departmental spending included in the 1994 Budget (Canada, Department of Finance, 1994). The review required ministers in each department to evaluate their programs using six tests:

1. serving the public interest
2. necessity of government involvement
3. appropriate federal role
4. scope for public sector/private sector partnerships
5. scope for increased efficiency, and
6. affordability.

The Program Review led to a significant structural change in the federal government's involvement in the Canadian economy, including:

- changes to the federal government's involvement in large aspects of Canada's transportation system;[24]
- a complete change to the federal government's approach to agriculture, including a move away from income support to income stabilization:[25]
- a reduction in the federal government's involvement in the business sector, including a proposed 60% cut in business subsidies;[26]
- an increased focus on efficiency in government departments and the manner in which they delivered services to Canadians.

Table 2 summarizes the reductions proposed for various departments through the Program Review process. The results clearly show a prioritization of then-existing spending. Large reductions in spending were required

24 There was a marked shift in the role and responsibilities of Transport Canada. Instead of owning, operating, and subsidizing the transportation system, Transport Canada began developing policies, regulating transportation, and enforcing safety standards. Some of the reforms included transferring airport management and, indeed, ownership to local authorities, privatizing the Air Navigation System (NavCan), and eliminating subsidies for farmers and transportation companies.

25 The 1995 Budget included measures to reduce federal support of agricultural safety nets by 30% over three years, cut subsidies to milk producers of 30% over two years, reduced federal spending on inspection and regulation, closed seven research facilities, and ended the Feed Freight Assistance transportation subsidy.

26 Resources remaining for supporting business would largely be in the form of loans and repayable contributions rather than subsidies.

Table 2: Proposed reductions in department spending based on the Program Review

	Spending (billions)		**Reductions**	
	1994/95	1997/98	$ billions	percent
Natural Resource Sector	4.8	3.3	−1.5	−31%
Agriculture	2.7	1.6	−1.1	−40%
Fisheries and Oceans	0.8	0.6	−0.2	−27%
Natural Resources	1.3	0.6	−0.6	−49%
Environment	0.7	0.5	−0.2	−32%
Transport	2.9	1.4	−1.4	−51%
Industrial, Regional and Scientific Programs	3.8	2.4	−1.4	−38%
Industry	1.3	0.7	−0.6	−43%
Science and Technology Agencies	1.4	1.0	−0.3	−24%
Regional Agencies	1.1	0.6	−0.6	−49%
Justice and Legal Programs	3.3	3.1	−0.2	−5%
Justice	0.8	0.7	−0.1	−8%
Solicitor General	2.5	2.4	−0.1	−4%
Heritage and Cultural Programs	2.9	2.2	−0.7	−23%
Foreign Affairs	4.1	3.3	−0.8	−19%
Foreign Affairs/International Trade	1.5	1.2	−0.3	−17%
International Assistance Envelope	2.6	2.1	−0.5	−21%
Social Programs	13.0	12.0	−1.0	−8%
Citizenship and Immigration	0.7	0.6	−0.1	−9%
Health	1.8	1.7	−0.1	−4%
Human Resources Development	2.5	1.7	−0.9	−35%
Indian Affairs and Northern Development	3.8	4.2	0.4	12%
Canada Mortgage and Housing	2.1	1.9	−0.2	−9%
Veterans Affairs	2.1	1.9	−0.2	−11%
Defence/Emergency Preparedness	11.6	9.9	−1.6	−14%
General Government Services	5.0	4.1	−0.8	−17%
Parliament/Governor General	0.3	0.3	0.0	−10%
Total	51.9	42.1	9.8	19%
Percent of GDP	7%	5%		

Notes: Numbers may not add due to rounding or the exclusion of other relatively minor line items.

Source: Canada, Department of Finance, 1995b.

of some departments, including Transport (51%), Natural Resources (49%), Agriculture (40%), and Industry (43%). Fairly small reductions were asked of others, including Health (4%), Citizenship and Immigration (9%), and the Canada Mortgage and Housing Corporation (9%). In fact, all departments outside of Justice and Social Programs were reduced by over 10%. In addition, major changes and reductions were made in Employment Insurance.[27]

The enactment of meaningful reductions in nominal spending coupled with fairly stable revenues meant that the federal government achieved its objective of a balanced budget quickly—two years later, in 1997/98. Figure 19 shows federal budget revenues and total spending as a share of GDP. What is clear from figure 19 and critical for understanding the current situation is that a balanced budget was achieved almost entirely through reductions in spending. Prior to the major tax cuts announced in the 2000 Budget,[28] budget revenues were fairly stable, ranging from 17.0% to 18.2% of GDP.

The achievement of budget surpluses was not short-lived. As illustrated in figures 20a and 20b, the federal government had budget surpluses consistently from 1997/98 to 2007/08. Figure 20a shows the nominal value of surpluses while figure 20b shows the value of deficits and surpluses as a share of GDP. In dollar terms (figure 20a), the surpluses over this period ranged from \$1.5 billion in 2004/05 to \$19.9 billion in 2000/01. These surpluses were used to reduce the net debt of the country. As a share of the economy, the surpluses ranged from 0.1% in 2004/05 to 1.8% in 2000/01. It is clear by both measures that the federal government was able to maintain the balance between spending and revenues to ensure budget surpluses.[29]

The ongoing surpluses meant that the federal government was able to reduce the outstanding stock of federal debt. The decline in the nominal value of federal debt is stunning: the value of federal debt (nominal) drops from a high of \$562.9 billion in 1996/97 to \$457.6 billion by 2007/08 (figure 21a). Equally as impressive, the federal debt as a share of GDP declined from

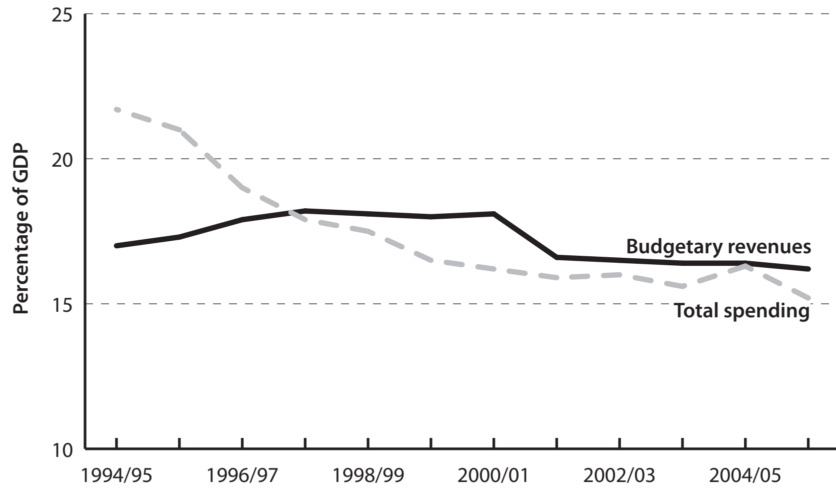
---

27 While Employment Insurance benefits were cut, the government was slow to reduce the contribution rates (payroll tax). The notional "surplus" of employment insurance, which refers to the difference between the revenues collected from the tax and the benefits paid out under the plan, contributed significantly to the elimination of the deficit because both the revenues and spending are included in the general federal budget. The Canada Pension Plan is markedly different, since both revenues and spending are segregated from the government's general budget.

28 Canada, Department of Finance, 2000; for a summary of the five-year tax reduction plan, see chapter 4, also available at <http://www.fin.gc.ca/budget00/tax/tax1-eng.asp>.

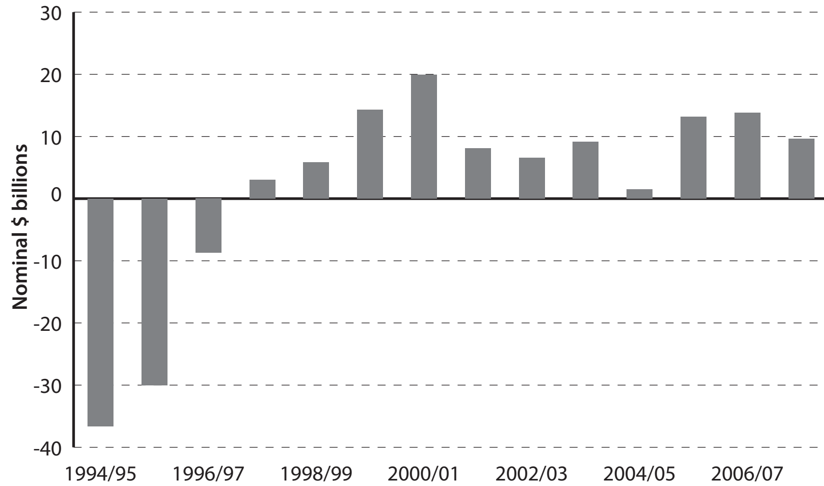
29 Paul Martin explained the rationale for government to remain in budget surplus regardless of economic situation more succinctly and convincingly than almost any economist. In his autobiography, he argued that, once government ran a deficit (i.e., borrowed money to finance part of its spending), it would quickly become addicted to using deficits to finance greater spending because it is politically expedient and easier. Such situations were to be avoided at all costs given the pain of achieving a balanced budget (Martin, 2008).

Figure 19: Federal total revenues and spending (percentage of GDP), 1994/95–2005/06



Source: Canada, Department of Finance, 2010c.

Figure 20a: Federal deficit/surplus (nominal $ billions), 1994/95–2007/08

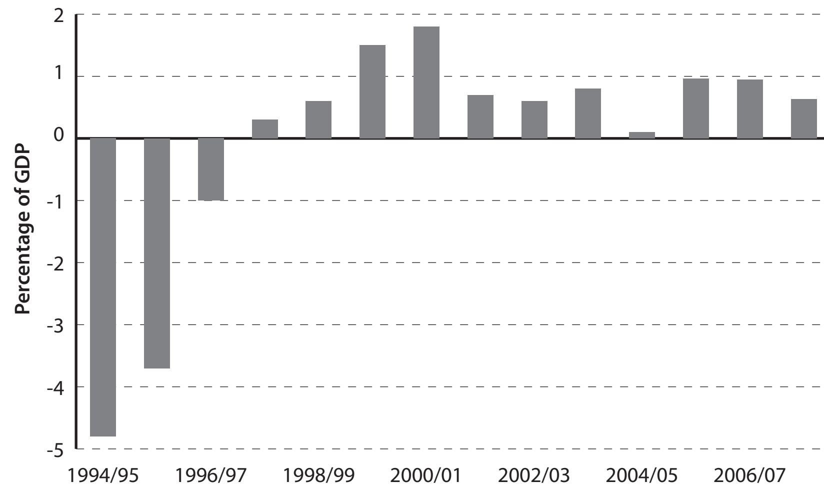


Source: Canada, Department of Finance, 2010c.

68.4% of GDP in 1995/96 to 29.9% of GDP in 2007/08 (figure 21b). Recall the research of Reinhart and Rogoff showing that, when accumulated debt exceeds a threshold of 90% of GDP, economies tend to have slower economic growth and its related costs (Reinhart and Rogoff, 2009). The substantial declines in Canadian federal debt, particularly in comparison to the size of the economy (GDP), had the opposite effect and Canada began to enjoy the benefits of lower debt burdens.

A clear benefit from the return to fiscal balance and the reduction of federal debt was a marked decline in interest charges. The nominal value of interest charges for the federal government declined from a high of $49.4

Figure 20b: Federal deficit/surplus (percentage of GDP), 1994/95–2007/08



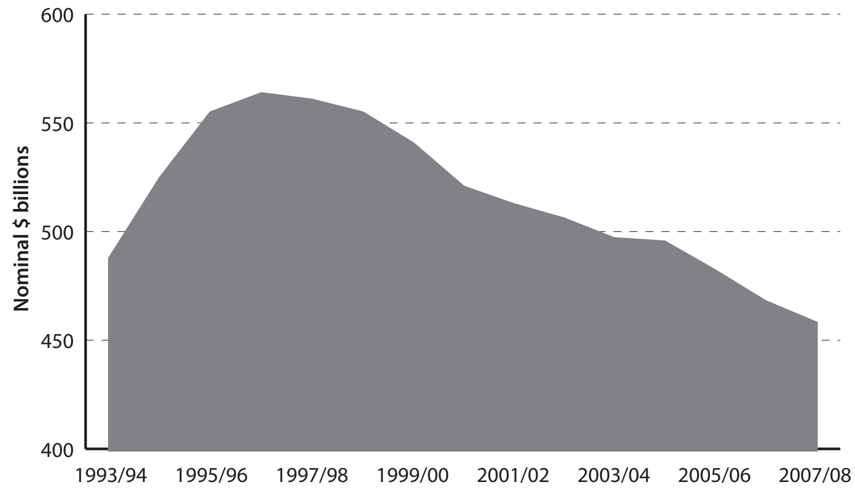
Source: Canada, Department of Finance, 2010c.

billion in 1995/96 to $29.4 billion in 2009/10 (figure 22a). Indeed, the benefits of reduced interest payments as a result of surpluses and debt reduction extended well into the current crisis as there were more resources available to the federal government for spending and tax relief without increasing total spending. In other words, the decline in interest charges, which reduces the wedge between total spending and program spending, allows for greater program spending without increasing total spending. The reduction in the wedge between total resources collected and the amount available to be spent on programs is illustrated in figure 22b: interest charges as a share of budget revenues declined from a high of 35.2% in 1995/96 to 13.3% in 2008/09. These charges have since begun to rise, though they have not yet come anywhere near the crisis levels seen in the mid-1990s.

Conclusion

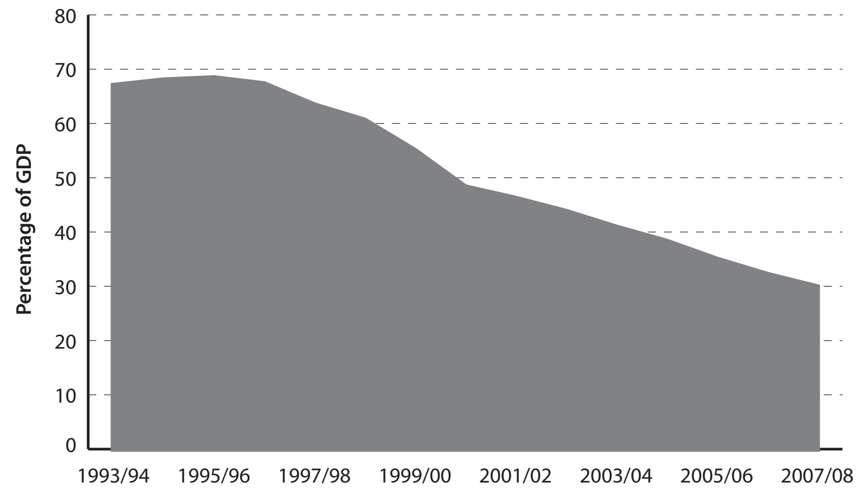
The federal Liberal Party undertook deliberate and difficult steps, namely cutting spending and public-sector employment in order to solve the deficit and debt problems of the country. They avoided the mistakes of the preceding decade and a half and took effective action. Their approach resulted in meaningful achievements in a short time, including balanced budgets, declining debt, and decreasing interest costs. In addition, they established a benchmark process for reviewing, prioritizing, and reducing government spending through their expenditure review program (1994 and 1995). Their efforts made Canada's economic position one envied around the world by political leaders who marveled at the fiscal turn-around and its benefits (*The Economist*, 2003, Sept. 25).

Figure 21a: Federal debt (nominal $ billions), 1993/94–2007/08



Note: There are several series available for measuring federal debt. The series chosen for this study is accumulated deficits, which measures gross or total debt minus financial and non-financial assets.
Source: Canada, Department of Finance, 2010c.

Figure 21b: Federal debt (percentage of GDP), 1993/94–2007/08



Note: There are several series available for measuring federal debt. The series chosen for this study is accumulated deficits, which measures gross or total debt minus financial and non-financial assets.
Source: Canada, Department of Finance, 2010c.

Figure 22a: Federal interest charges (nominal $ billions), 1993/94–2009/10

Source: Canada, Department of Finance, 2010c.

Figure 22b: Federal interest charges (percentage of budget revenues), 1993/94–2009/10

Sources: Canada, Department of Finance, 2010c; calculations by authors.

4 Applying the lessons of the 1990s today

It should be clear that the federal governments struggled with the same fiscal problems during the 1980s and early 1990s that confront them today.[30] Unfortunately, the current federal government is relying on the same failed plan. Rather than undertake the difficult task of reducing spending immediately in order to achieve a balanced budget, as the Liberal Party did in 1995, the current government is instead relying on longer-term spending restraint coupled with expectations of stronger revenue growth to solve its deficit problem. The same risks observed in the period from 1980 to 1995 are present now: a failure to restrain spending adequately, higher debt charges, and lower-than-expected revenue growth. Indeed, we already see some evidence that the federal government is having difficulty restraining spending increases and that revenues are not being generated as budgeted.

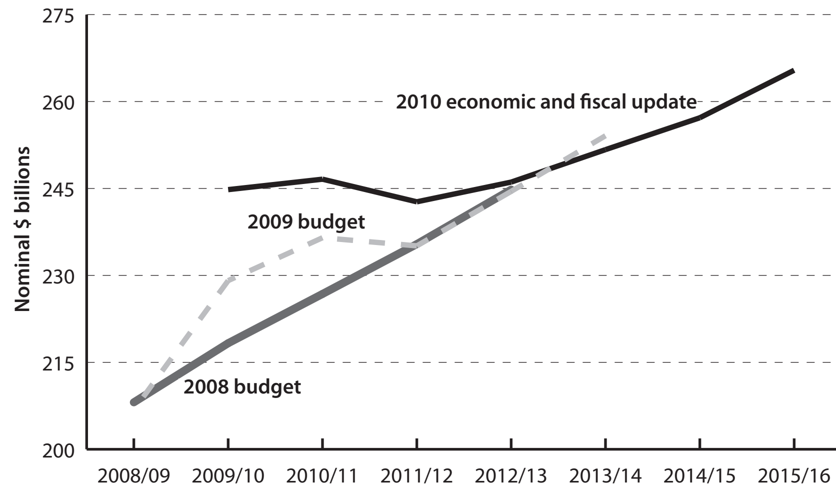
Figure 23 shows the program-spending plans of the federal government based on the last three budgets (Canada, Department of Finance, 2008, 2009, 2010a).[31] Two aspects of the Budgets shown in figure 23 are worth noting. The first is the nature of the stimulus spending introduced in the 2009 Budget, which deviates from the 2008 spending plan in the limited, temporary manner that is normal for stimulus spending. The 2009 Budget

---

30 This study compares periods using government statistics such as government spending, deficits, debt, and interest costs. This narrow focus has been chosen to show the parallels between the problems of the 1980s and 1990s and those of the current situation and how solutions from the 1990s can be applied today. It is important to acknowledge, however, that there are a host of non-government statistics such as interest rates and foreign exchange that also influence economic performance. The conditions these macroeconomic indicators record vary between the periods discussed. For example, governments in the 1980s, 1990s, and 2000s faced very different interest rates: on a monthly basis, the 1-month Treasury-Bill interest rate ranged from 6.8% to 21.3%, with an average of 11.1% during the 1980s. During the 1990s, the same rate ranged from 2.5% to 13.7% with an average of 6.1%. The rates ranged from 0.1% to 5.5% with an average of 2.9% during the 2000s (up to May 2010) (Statistics Canada, 2010b). Nevertheless, the existence of these macroeconomic differences does not falsify the fundamental argument of this study that the budgetary approach of the 1990s was successful and that of the 1980s a failure.

31 Please note that the *Update of Fiscal and Economics Projections, October 2010* (Canada, Department of Finance, 2010d) was used for the revised 2010 forecasts rather than *Budget 2010* (Canada, Department of Finance, 2010a) because it presents the most up-to-date expectations of the federal government.

Figure 23: Federal program spending plans (nominal $ billions), 2008–2010 Budgets



Note: The figures above do not include spending on interest costs.
Source: Canada, Department of Finance, 2008, 2009, 2010d.

introduced limited and temporary spending for 2009/10 and 2010/11 and called for a return to the pre-stimulus level of program spending planned in the 2008 budget for 2011/12 and 2012/13.[32]

The second notable aspect of the Budgets shown figure 23 is the new higher level of spending introduced in the recent 2010 economic update. This most recent spending plan announced by the federal government departs permanently from the post-stimulus spending planned in the 2009 Budget. For example, program spending in the 2009 Budget was scheduled to be $235.1 billion in 2011/12 after the stimulus was exhausted. The 2010 Update increases program spending in 2011/12 to $242.7 billion, an increase of 3.2% on top of the stimulus spending. In other words, the federal government has now proposed a permanently higher level of program spending based on the level of program spending established in the stimulus plan of 2009. The failure to control growth in spending illustrated in figure 23 is reminiscent of the experience of the 1980s and 1990s. The problems in the government's plan are made even more serious when revenues are considered.

Figure 24 illustrates the federal government's expectations of budget revenue outlined in the 2009 and 2010 Budgets as well as the *Update of Economic and Fiscal Projections, October 2010* (Canada, Department of Finance, 2009, 2010a, 2010d). Each of these Budgets reduced the current and future revenues expected by the federal government, which, in each

32 The 2008 Budget indicates program spending of $235.4 billion and $244.8 billion in 2011/12 and 2012/13, respectively (Canada, Department of Finance, 2008). By comparison, the 2009 Budget contains program spending of $235.1 billion and $244.5 billion in 2011/12 and 2012/13, respectively (Canada, Department of Finance, 2009).

successive budget update, had to lower its forecast for future revenues. The revisions are not incidental: for instance, the federal government reduced its four-year revenue forecast by $16.3 billion between the spring 2010 budget and the fall 2010 update. This mirrors budgets of the period from 1980 to 1995 when the federal government was unable to control growth in spending over time and had to revise its revenue expectations downward from budget to budget. The result of this failure was continuous deficits that led to increases in federal debt and interest costs.

The lesson is that it is prohibitively difficult to achieve balanced budgets by simply restraining growth in spending over long periods of time and hoping that revenue growth closes the gap. The success of the 1995 Budget in dealing with the federal government's last deficit and debt problem teaches us that spending cuts implemented over a few years lead to a quick resolution of deficits and sets the stage for a virtuous cycle of fiscal surplus, debt reduction, and declining interest charges.

The federal government should heed the lessons of the 1995 Budget and move deliberately in its next budget to reduce spending in order to eliminate the deficit in the near term. Two broad types of spending reductions are recommended.

1 Return program spending to level planned in pre-stimulus budgets

The first reduction to be made is a return to the levels of program spending planned before the stimulus spending introduced for 2009/10 and 2010/2011.[33]

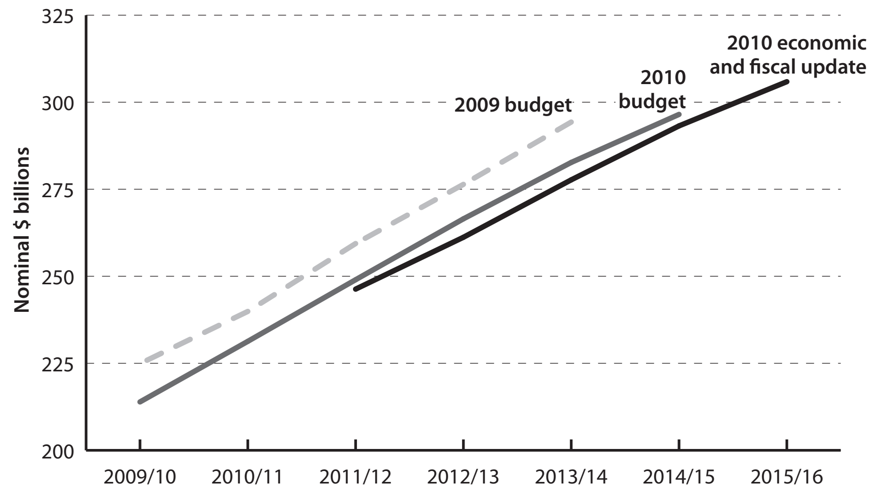
---

33 Some may question why tax increases are not considered and, indeed, the current leader of the federal Liberal Party, Michael Ignatieff, has repeatedly called for scheduled reductions in the corporate income tax to be frozen in order to eliminate the budget deficit. The use of tax increases to close budget deficits is questionable for three reasons. First, it assumes that higher tax rates result in higher tax revenues. The relationship between tax rates and revenues is not that simple and, indeed, in many cases raising tax rates can actually result in lower tax revenues. This is a simplistic view of taxes and tax revenues because it ignores the base upon which the tax rate is applied and any incentive effects the increased tax rate may have on people's behaviour and the tax base itself. For example, a lower tax rate that encourages the growth of the tax base can reasonably be expected to generate more tax revenue over time than a higher tax rate, which retards economic growth and thus the tax revenues extracted from the underlying base.

Second, it assumes that any higher revenues flowing from higher tax rates—again if higher revenues materialize—will be used to eliminate the deficit rather than finance additional new spending. There are many examples, both in Canada and outside—particularly in European countries—showing that higher tax revenues from increased tax rates are largely used to finance additional spending rather than eliminate the deficit.

Third, one must consider Canada's tax competitiveness and the effect higher tax rates would have on economic performance. Of particular importance are taxes such as corporate and personal income taxes, which are strongly related to investment. Increases in these tax rates will deter investment, which has broad implications for economic performance.

Figure 24: Revised estimates for federal budget revenues (nominal $ billions), 2009–2010 Budgets



Sources: Canada, Department of Finance, 2009, 2010a, 2010d; Canada, Receiver General for Canada, 2010.

Stimulus spending is supposed to be temporary and, once it is completed, spending should return to its pre-stimulus level, adjusting for normal growth over time.[34] If program spending does not return to its pre-stimulus level, as has been the case in Canada and many other countries,[35] then the stimulus was not really stimulus but simply more permanent government spending. Figure 25 shows federal program spending beginning in 2002/03 through to 2015/16 (Canada, Department of Finance, 2010c, 2010d). The effect of the stimulus is evident: program spending spikes from $207.9 billion in 2008/09 to $244.8 billion in 2009/10. However, post-stimulus program spending does not return to its pre-stimulus level but simply grows from the new base established by the stimulus spending. The stimulus spending was not, therefore, temporary but rather permanent additional spending.

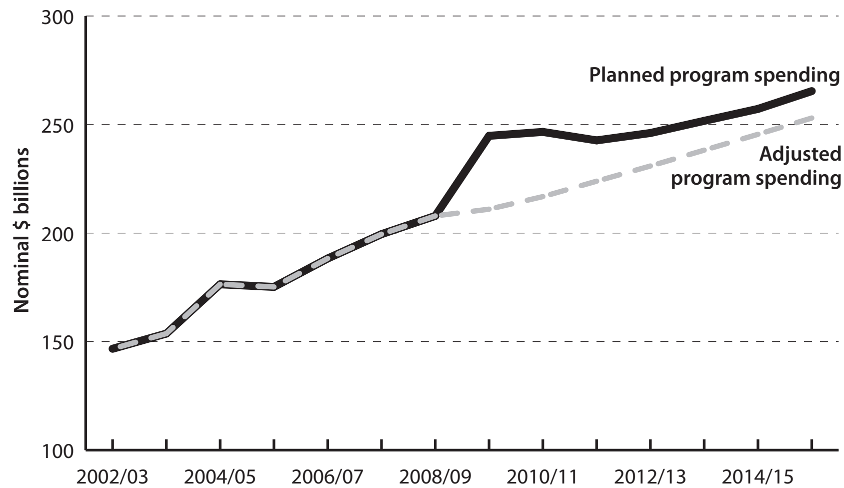
The divergence between the pre-stimulus level of program spending and the new higher base of program spending is illustrated in figure 25. Adjusted program spending (dashed line) is calculated by increasing the

For an analysis of the errors in Mr Ignatieff's view of corporate income-tax rates, see Lammam and Veldhuis, 2010; for an excellent and succinct discussion of the link between investment and economic performance, see Stanford economics professor John Taylor's recent discussion of this topic on his blog (Taylor, 2011, January 14); for a review of scholarly material on the relationship, see Murphy and Clemens, 2010: pp. 17–26; and Palacios and Harischandra, 2008.

34 "Normal" in this instance could refer to growth rates observed over the previous five or even 10 years or, more conservatively, to growth rates constrained by the rate of economic growth or population growth coupled with inflation.

35 Perhaps the most poignant case of a government using stimulus as a rationale to implement significantly greater permanent spending is the US federal government in 2008 and 2009; see the Congressional Budget Office's latest analysis, *Long Term Budget Outlook* (US-CBO, 2010).

Figure 25: Planned federal program spending compared to lower-growth program spending adjusting for the stimulus (nominal $ billions), 2002/03–2015/16



Note: The figures above do not include spending on interest costs.
Sources: Canada, Department of Finance, 2008, 2010c, 2010d; Canada, Receiver General for Canada, 2010; Statistics Canada, 2010e; calculations by authors.

pre-stimulus level of program spending (2008/09) by the annual rate of population growth and inflation. The gap between actual planned spending and the spending that might have occurred without the stimulus is $18.8 billion in 2011/12. This is 63.1% of the expected deficit in that year, an important fact since it means a substantial portion of the near-term deficit can be eliminated by imposing a fiscal discipline that ensures the temporary stimulus spending be temporary, rather than permanent.

Thankfully, the depth of the current financial problem faced by the federal government is not as severe as was experienced in the 1980s and early 1990s. Fiscal year 2012/13 was chosen as the target year to achieve a balanced budget based on the two-year time horizon, which was also used by the Chrétien Liberals in 1995. Reductions in program spending totaling $15.7 billion by 2012/13 (compared to 2010/11) are required to bring program spending in line with pre-stimulus levels after adjusting for population growth and increases in prices. The reduction in program spending of $15.7 billion (2012/13) represents a 6.3% reduction in program spending compared to 2010/11 program spending (forecast). To put this reduction in context, the federal government calculated stimulus spending of $22.7 billion and $17.2 billion in 2009/10 and 2010/11, respectively. Another way to think about the size of the proposed reductions is to compare it with the reductions introduced by the Liberal Party in 1995, which totalled nearly 10% over two years. The details of the revised fiscal plan are summarized in table 5 (p. 49).

Table 3 gives a categorical summary of the components of the stimulus spending implemented in 2009/10 and 2010/11. The stimulus plan includes

Table 3: Summary of Stimulus Action in 2009 Federal Budget ($ millions)

	2008/09	2009/10	2010/11
Improving access to financing and strengthening Canada's financial system		162	12
Action to help Canadians and stimulate spending	695	5880	6945
Action to stimulate housing construction	530	3865	1395
Immediate action to build infrastructure		5727	5055
Action to support businesses and corporations	12	2372	2121
Plus:			
Capital spending (cash adjustments)		697	685
Loans			
Auto Sector		2700	
Municipalities for Housing-related Infrastructure		1000	1000
Timing of Home Renovation Tax Credit		500	
Total Federal Stimulus		22,742	17,200
Total Stimulus with Leverage		29,298	22,316

Source: Canada, Department of Finance, 2009: table 1.2.

direct spending, tax relief, and additional transfers to individuals, including enhanced Employment Insurance benefits, additional jobs training and placement programs, First Nations initiatives, programs aimed to stimulate the housing sector, infrastructure spending, research and development subsidies, regional subsidies, and new spending on industry, culture, tourism, and the environment.[36] The reduction in program spending of $15.7 billion (6.3%) by 2012/13 can be achieved a number of ways, including proportionately reducing stimulus spending that is now included in permanent spending, an across-the-board reduction in spending, or by reviewing and prioritizing spending as the Liberals did in 1994 and 1995.[37]

36 For information on the 2009 stimulus plan, see Canada, Department of Finance, 2009. Table 1.2 provides a financial summary, tables 3.5, 3.6, 3.7, and 3.8 provide overviews of the various components of the stimulus, and chapter 3 provides both financial and operational details concerning the stimulus plan.

37 There are a number of initiatives included in the stimulus plan that should be extended and made permanent. For example, the 2009 Budget reduced import tariffs on a range of machinery and equipment, making it more economical for Canadian businesses to invest and develop their enterprises in Canada. See Canada, Department of Finance, 2009: 169 for a summary of the tariff relief program. Table 3.8 (p. 185) indicates a two-year cost estimate of $169 million, which is a fairly small program that offers enormous economic advantages and benefits. This

Table 4 gives a sampling of the many programs and initiatives included in the 2009 stimulus plan with a brief description and price tag (based on 2010/11 cost estimates). Some of the programs seem quite distant from a stimulus-type initiative meant to encourage immediate consumption. Indeed, many of the programs included seem more like additional permanent spending than they do temporary programs and this may be part of the explanation for the federal government's inability to return program spending to pre-stimulus levels. On the other hand, some of these programs may be worth continuing. This is why the federal government should replicate the review process used in 1994 and completed in 1995 to prioritize federal spending.

The plan outlined in table 5 (p. 49) shows program spending being reduced by $7.8 billion in 2011/12 compared to 2010/11 levels. Program spending is reduced by an additional $7.9 billion in 2012/13, based on the revised program spending for 2011/12.[38] It is assumed that much of the stimulus spending initiated in 2009 is eliminated or that equal amounts of offsetting cuts in other spending are identified. While substantial, these reductions based on bringing program spending back in line with what would have been the likely level of program spending based on pre-stimulus spending do not eliminate the entire deficit by 2012/13. An additional $6.2 billion in spending must be cut in order to achieve a balanced budget in 2012/13.

There are two options available to the federal government. The first is to review existing spending after stimulus-related spending is eliminated, looking for ways to reduce federal program spending that existed prior to the increase in program spending associated with the stimulus program. There are a number of areas where the federal government could find substantial savings. For instance, a number of studies have analyzed the wastefulness and inefficiency of subsidizing corporations (Milke, 2008; 2009). Another area where savings are likely to be found are the various regional development agencies, whose budgets were increased substantially over recent years. A second and more fundamental option for eliminating the deficit over the coming two years involves realigning the way in which Canada's public health care system is financed and regulated.

---

and other initiatives make sense regardless of the country's economic situation and should be extended because they make Canada more attractive for investment and entrepreneurship.

38 There are many ways to implement the two-year reduction of $15.7 billion. The plan presented in table 5 (p. 49) distributes the cuts evenly between 2011/12 and 2012/13. One could easily make the case for front–loading or back-loading the reductions. The key, however, for the plan presented in table 5 is the reduction of program spending by $15.7 billion by 2012/13, which brings program spending back in line with what would have been the case had pre-stimulus program spending increased based on population growth and inflation.

Table 4: Sampling of programs and initiatives in the 2009 Stimulus Action

Program	Estimate
extension of EI benefits to 50 weeks from 45 weeks[1]	$575 million
EI benefits for Canadians in long-term training	$250 million
increased training funding for EI generally	$500 million
job training for individuals not qualified for EI	$250 million
increases to National Child Benefit Supplement and Canada Child Tax Benefit[2]	$310 million
enhancing the Working Income Tax Benefit[3]	$580 million
targeted tax relief for seniors	$340 million
enhancing energy efficiency	$150 million
first-time homebuyer's tax credit	$180 million
funds for renovating and retrofitting social housing	$500 million
housing funds for low-income seniors, persons with disabilities, First Nations, and Northern housing	$1.1 billion
green infrastructure	$200 million
infrastructure stimulus	$2.0 billion
contributions and support for Building Canada Fund[4]	−$250 million
funding for recreational facilities	$250 million
on-reserve infrastructure funding	$255 million
knowledge initiatives, including infrastructure for universities and colleges, the Canada Foundation for Innovation, and modernizing laboratories	$1.25 billion
extending broadband services to rural areas	$100 million
federal infrastructure programs	$254 million
support for specific sectors of the economy, including forestry, agriculture, slaughterhouses, shipbuilding, and space technologies	$330 million
additional support for the Canada Television Fund	$100 million
promotion of "Marquee Festivals"	$50 million
support for Green Energies	$200 million
regional business support and subsidies	$731 million

Notes: The estimates were taken from the stimulus plan in Budget 2009 (Canada, Department of Finance, 2009). The list in the text totals $10.7 billion in spending in 2010/11. [1] For information on Canada's Employment Insurance system, including the new programs added under the 2009 stimulus, see <www.servicecanada.gc.ca/eng/sc/ei/index.shtml>. [2] For information on the National Child Benefit Supplement, see <www.nationalchildbenefit.ca/eng/home.shtml>; for information on the Canada Child Tax Benefit, see <www.cra-arc.gc.ca/bnfts/cctb/menu-eng.html>. [3] For information on the Working Income Tax Benefit (WITB), see <www.cra-arc.gc.ca/bnfts/wtb/menu-eng.html>. [4] For information on the Building Canada Fund, including details about the Green Infrastructure Fund, infrastructure stimulus fund, and communities components, see <www.buildingcanada-chantierscanada.gc.ca/funprog-progfin/target-viser/bcf-fcc/bcf-fcc-eng.html>.

Source: Canada, Department of Finance, 2009.

2 Reforming provincial health transfers

The second component of the proposed reform would bring a fundamental change in the relationship between the federal and provincial governments with respect to the way in which Canada's public health care system is financed and regulated. Like the first recommendation, this reform is based on our country's experience in the 1990s.

Restructured and reduced provincial transfers—experience from the 1990s

The 1995 Budget brought a major restructuring and reduction in federal transfers to the provinces. The budget began a transition away from federal transfers based on federal-provincial cost sharing to block grants. Prior to the 1995 Budget, the federal government provided two major transfers to the provinces for programs: the Established Program Financing (EPF) and the Canada Assistance Plan (CAP).[39] The Established Program Financing (EPF) was a block transfer to the provinces to support health and post-secondary education in the provinces. It was distributed to the provinces regardless of provincial spending in these areas. The Canada Assistance Plan (CAP) was a cost-sharing program in which the federal government paid up to half of the amount spent by provincial governments on social services. One of the problems with this approach is the incentives imbedded in it for additional spending regardless of its efficacy. In this situation, the provinces could finance an extra dollar of spending on social programs with just 50 cents of provincial revenue. The federal government provided the remaining funds. Critically, this meant that the federal government did not directly control the growth of this federal spending.

The 1995 Budget replaced the Canada Assistance Plan (CAP) and the Established Program Financing (EPF) with a new block transfer known as the Canada Social Transfer—renamed the Canada Health and Social Transfer (CHST) in the 1996 Budget—starting in 1996/97.[40] As a result, the negative incentives embedded in the cost-sharing agreement of the Canada Assistance Plan were eliminated. Figure 26 illustrates the transfer payments under the old EPF and CAP programs compared to the revised payments made under the Canada Health and Social Transfer (CHST). The 1995 Budget included a reduction in the total amount transferred to the provinces. The EPF and CAP transfers combined were set to fall from $29.3 billion in 1996/97 to $25.1 billion in 1997/98.[41]

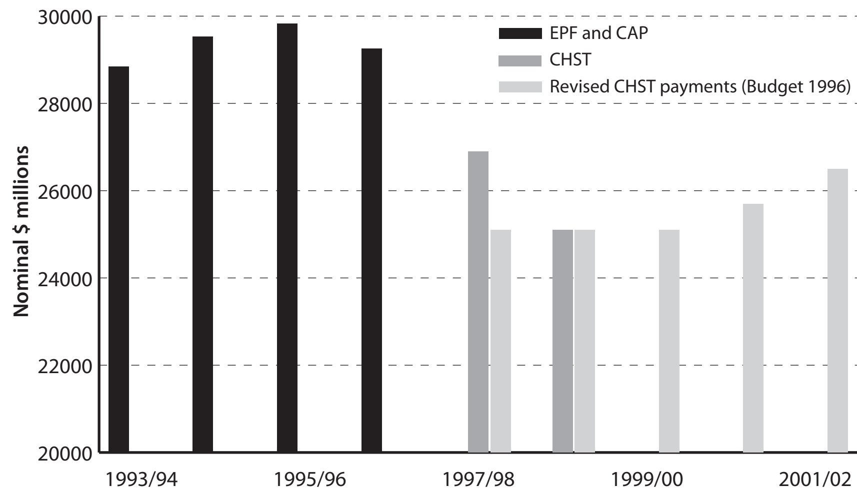
---

39 These two transfer programs supported program spending on health care, post-secondary education, and welfare. They are distinct from the Equalization Program, which is meant to smooth over differences in the provinces' ability to raise own-source revenues. For information on Canada's equalization system, see Clemens and Veldhuis, 2007; and Clemens, Veldhuis, and Palacios, 2007.

40 For a history of the CHST, see <http://www.fin.gc.ca/fedprov/his-eng.asp>.

41 In percentage terms, the reduction in provincial transfers was larger than the reductions applied to federal programs.

Figure 26: Transfer payments (nominal $ millions) under EPF/CAP and CHST, 1993/94–2001/02



Note: EPF = Established Program Financing; CAP = Canada Assistance Plan; CHST = Canada Health and Social Transfer.
Sources: Canada, Department of Finance, 1994: table 9; Canada, Department of Finance, 1995a, 1995b, 1996.

The introduction of a single block grant also allowed and, indeed, encouraged the provinces to pursue innovation and improved performance through experimentation based on the increased flexibility and autonomy accorded them by the federal government.[42] Under the cost-sharing arrangements, the federal government had controlled standards for social services by connecting the payment of transfers to the provinces to adherence to national standards. This centralized approach and federal regulation meant that provinces were, to a certain extent prohibited—or at least inhibited—from experimenting with alternative delivery models. Indeed, Finance Minister Paul Martin noted in his historic presentation of the 1995 Budget that "the restrictions attached by the federal government to transfer payments in areas of clear provincial responsibility should be minimized ... they limit innovation ... increase administrative costs" (Martin, 1995: 17–18).

Canadian welfare reform—decentralization and incentives matter

The CHST reform set off a period of innovation and experimentation across the country in terms of both welfare design and delivery. The reduced transfers coupled with greater provincial autonomy and responsibility for welfare and its costs meant that the provinces had the incentive and authority to

42 For a discussion of the reforms in the federal transfers, see Veldhuis and Clemens, 2003.

design and deliver better programs.[43] The following section highlights the diversity of reforms across the country.[44]

Alberta was the first province to reform welfare in a meaningful way. In 1993, Alberta overhauled the administration of the Alberta Family and Social Services Ministry.[45] One of the main avenues of reform was focused on diversion. That is, the government shifted the emphasis in the Ministry away from administrative tasks such as determining eligibility and mailing payments to proactively trying to prevent people ("diverting") from entering welfare before other possibilities, including employment, were exhausted. The premise of the change was based on the fact that once people enter the welfare system, they have a much higher probability of using it again in the future. Thus, people were helped by making sure that every other possible alternative (like finding or staying in work) was exhausted before they could enter the welfare bureaucracy. The combination of focusing on alternatives to welfare and bringing benefit levels in line with low-paid employment resulted in reductions in welfare dependency and generally improved outcomes for former welfare recipients. One study concluded that almost half of the 172,000 people who left the province's welfare rolls between 1993 and 1996 found full-time employment (Elton, 1997; Canada West Foundation, 1997).

Ontario's welfare system had profound problems during the 1990s.[46] In 1994, Ontario had the highest rate of social-assistance-to-population (12.8%) in the country, its spending was increasing at an unsustainable rate, and its benefit levels were encouraging ever higher rates of welfare. The newly elected government in 1995 immediately brought in a number of changes including reduced benefit rates, an increased focus on diversion to non-welfare alternatives, greater focus on employment, and administrative improvements. *Ontario Works*, introduced in 1998, was a formal and fairly broad "workfare" program that was unique in the Canada. The goal of the program was to help welfare recipients return to work. The work requirement was mandatory for

43 There were a number of common reforms adopted by most, if not all of the provinces. One common feature of reform was a reduction in benefit levels, particularly for single employable people. There was an increasing understanding that, when welfare benefits surpass comparable income available from low-paid work, incentives are created to enter or remain on welfare. Many of the reductions in benefit levels and particularly those for single employable people were aimed at re-establishing a balance between welfare benefits and the income available to workers from low-paid work. For an empirical examination of the relationship between benefit levels and welfare rates during the 1990s, see Emes and Kreptul, 1999.

44 This section is largely based on the summary of provincial welfare reform presented in Fiscal Reforms: Unsung Provincial Heroes, chapter four in Crowley, Clemens, and Veldhuis, 2010. It also relies on Schafer, Emes, and Clemens, 2001.

45 For a summary analysis of the reforms adopted in Alberta, see Boessenkool, 1997.

46 For a discussion of the problems in the welfare system prior to its reform, see Richards, 1997; for a detailed examination of Ontario's welfare system, see Sabatini, 1996.

all employable adults. The result of the reforms was a reduction in welfare dependency that exceeded the national trends (Finnie, Irvine and Sceviour, 2005; Roy, 2004; Schafer, Emes, and Clemens, 2001).

British Columbia was one of the last provinces to reform welfare. In 2001, a newly elected Liberal government moved quickly to implement wholesale changes to the province's welfare system (Clemens and Schafer, 2002). Most noticeable was the introduction of a rolling benefit time limit, which mirrored a US reform introduced in 1996. Each month a recipient received welfare benefits counted towards a 24-month limit within any five-year period.[47] The program became effective April 1, 2002.[48] The introduction of a rolling time limit essentially returned the program to being an insurance scheme rather than a source of permanent income.

The success of provincial welfare reforms across the country are hard to deny. Welfare dependency was reduced well beyond the cyclical level observed over the previous decade and a half. By 2000, for example, the number of welfare beneficiaries had decreased to slightly over 2 million (6.8% of the population) from a peak of 3.1 million (10.7% of the population) (Finnie, Irvine and Sceviour, 2005; Finnie and Irvine, 2008; Schafer, Emes, and Clemens, 2001). Welfare-related spending also declined and assisted governments across the country in balancing their budgets. Most importantly, the innovation and experimentation encouraged by the reform of federal transfers and regulations meant that provinces were doing a markedly better job of identifying problems and actually helping people back into the labour market.

Applying the lessons of welfare reform to health care

There is broad consensus that one of the serious issues facing Canada's governments both in the short and long term is the delivery and financing of health care. As was the case in 1995, Canada has an opportunity not only to put its financial house in order but also solve a related social problem, in this case improving health care for Canadians in a financially sustainable manner. The lessons of the success of the 1995 welfare reforms provide a framework for health care reform.[49]

---

47 Reaching the limit for employable individuals would result in fairly stiff reductions in benefits, to zero in some cases, while more difficult cases like families with children would suffer much smaller reductions in their benefits.

48 Please note that as the deadline for the first two-year period in the five-year window of benefit eligibility approached, the regulations regarding the penalties and deferrals were extended, which basically nullified the penalties and any sense of a real time limit on receipt of benefits (Gabel, Clemens, LeRoy, and Veldhuis, 2003).

49 This approach to deficit reduction and health reform was first contemplated, reviewed, and discussed as part of the writing of *The Canadian Century*. Credit is due our co-author Brian Lee Crowley who was integrally involved in those discussions and deliberations. For more information, see Laurier's Unfinished Symphony, chapter nine in Crowley, Clemens, and Veldhuis, 2010.

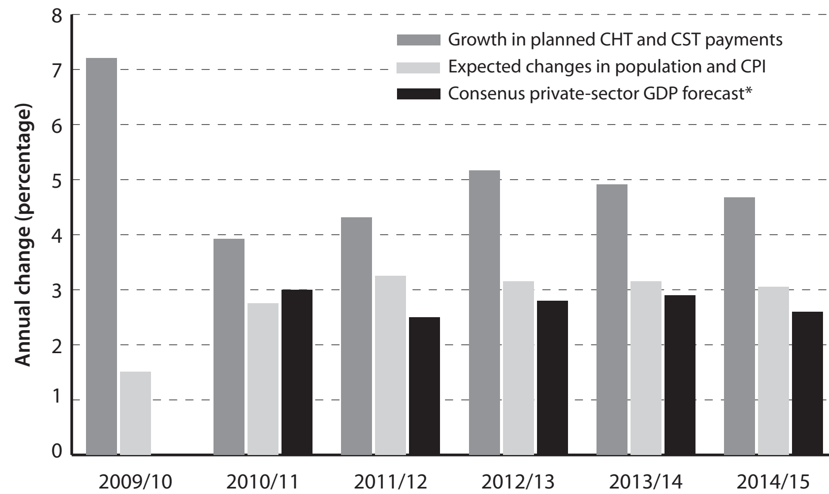
There are serious challenges facing the federal and provincial governments with respect to health care spending. Figure 27 illustrates the planned transfers from the federal government to the provinces for health care over the next five years. It is clear that health care transfers are growing at a rate well in excess of population and expected inflation as well as real GDP growth. In some years, such as 2012/13, the annual increase in the health-related payment is more than double the rate of expected GDP growth and almost double the rate of expected population growth and inflation.

The growth in the CHST also outstrips by a wide margin the growth in federal program spending. For example, the average growth in the CHST from 2010/11 through to 2014/15 is expected to be 4.6% while growth in total program spending over the same period is forecasted at 1.0%. A larger and larger share of program spending at the federal level is being dedicated to health-related transfers to the provinces and such spending increases are not sustainable without either raising taxes or reducing other spending (which is already occurring in relative terms), both of which have their own set of costs that need to be considered.

Canada has already experienced a relative reduction in non-health care spending at the provincial level in order to accommodate the near insatiable demand for health spending. Figure 28 illustrates the percentage of total program spending on health care for 1990/91 and 2008/09, the latest year of available data.[50] The total for Canada (all provinces) shows that health spending as a percentage of total program spending has increased from 30.3% in 1990/91 to 36.7% in 2008/09. Every province has experienced an increase in the portion of their budget devoted to health care. In Nova Scotia and Ontario, already over 40% of total program spending is being consumed by health care and a number of other provinces are close to this threshold (figure 28). It is also important to note that the growth in health spending is outstripping almost every other area of provincial spending (Kotlikoff and Hagist, 2005). The proportional increase in health spending compared to all other provincial spending coupled with the consistent high rate of annual growth in health care spending means that other categories of provincial spending will continue to be sacrificed in order to finance health care spending unless fundamental changes are introduced.

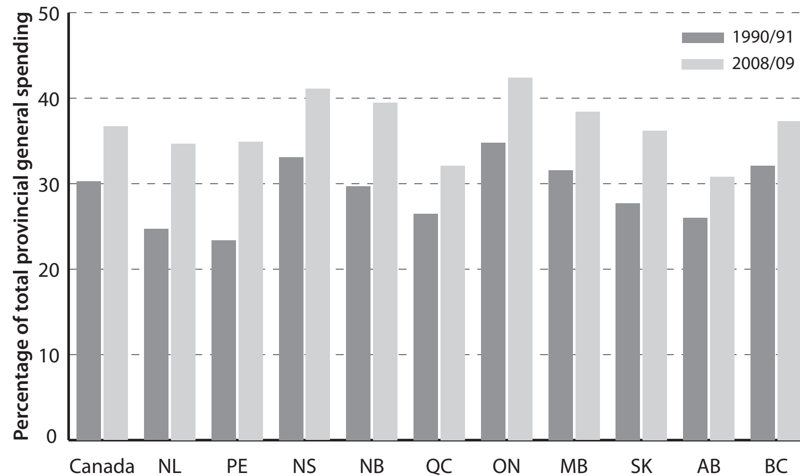
50 The series used in figure 28, which is provided by Statistics Canada, is referred to as the Financial Management System (FMS). Statistics Canada adjusts provincially provided numbers in order to accommodate differences in accounting among provinces so as to create a consistent and comparable pan-Canadian series of data. Unfortunately, this series has been cancelled and will be replaced by a new series of comparable data in the future. Another important source of information on health care used by many researchers is the Canadian Institute for Health Information (CIHI). See, for example, Canadian Institute for Health Information, 2010.

Figure 27: Expected growth in CHT and CST payments compared to expected changes in population and CPI, 2009/10–2014/15



Notes: CHT = Canada Health Transfer; CST = Canada Social Transfer.
* Consensus forecast as of the fall economic and financial update, October 2010. Population was forecast at 10-year average of 1.06% growth rate.
Sources: Canada, Department of Finance, 2010a: table 4.2.5; Canada, Department of Finance, 2010d: table 2.1; Statistics Canada, 2010a, 2010c; calculations by authors.

Figure 28: Provincial health care spending as a percentage of provincial general spending, 1990/91 and 2008/09



Note: Provinces of Canada and their acronyms: Alberta = AB; British Columbia = BC; Manitoba = MB; New Brunswick = NB; Newfoundland & Labrador = NL; Nova Scotia = NS; Ontario = ON; Prince Edward Island = PE; Quebec = QC; Saskatchewan = SK.
Source: Statistics Canada, 2010d; calculations by authors.

The other concerning aspect of health care is its quality and timeliness. As was the case with welfare before reform, it appears that Canadian governments spend substantial resources on health care while Canadians do not enjoy commensurate programs and benefits. Canada's health care system is, on an age-adjusted basis, the developed world's third most expensive after Iceland and the United States.[51] Canada's performance in delivering health care is not commensurate with this comparatively high level of spending. One area Canada where has repeatedly fallen short is waiting times for medical procedures. For example, the total waiting time between referral from a general practitioner and delivery of elective treatment by a specialist was 18.2 weeks in 2010,[52] an increase from 16.1 weeks in 2009. There was considerable variation among the provinces, ranging from a low of 14.0 weeks in Ontario to 44.4 weeks in Prince Edward Island (Barua, Rovere, and Skinner, 2010).

Part of the explanation for Canada's long wait times is a low supply of medical professionals and medical technologies. Canada's physician-to-population ratio of 2.2 (per 1,000 population) is one of the lowest (tied for 20th out of 22 countries) in the developed world. Similarly, Canada ranks 17th out of 26 countries for CT scanners (12.7 per million population) and 17th out of 25 countries for MRIs (6.7 per million population) (Rovere and Skinner, 2010). The relatively low access to modern medical technologies also shows up in wait times for these technologies. For instance, in 2010, for Canada as a whole, the wait time for an MRI was 9.8 weeks and 4.5 weeks for an ultrasound (Barua, Rovere, and Skinner, 2010). In addition, much of Canada's medical and diagnostic equipment is outdated and in need of replacement (Esmail and Walker, 2008).

Many of these findings are supported by the report, *Healthy Canadians*, which focuses on measuring health performance (Canada, Ministry of Health, 2008). For example, the report found that 83.0% of Canadians reported having a regular family doctor in 2007, down from 85.1% in 2003 (Canada, Ministry of Health, 2008: fig. 3). However, neither 85.1% nor 83.0% are impressive given the universal principle underpinning Canadian health care. Similarly, 25.3% of Canadians in 2007 reported difficulty obtaining immediate care and 17.2% reported difficulty in obtaining routine or ongoing health services.[53]

51 Health expenditures in Switzerland were the same as those in Canada in 2005 on an age-adjusted basis (Rovere and Skinner, 2010).

52 This calculation is averaged across 12 medical specialties and includes the 10 provinces. For more information, see Barua, Rovere, and Skinner, 2010.

53 The figures reported in 2007 represented increases from the 2003 report: the percentage reporting difficulty in obtaining immediate care increased from 23.8% in 2003 to 25.3% in 2007 and the percentage reporting difficulty in obtaining routine or ongoing health services increased from 16.4% in 2003 to 17.2% in 2007 (Canada, Ministry of Health, 2008: fig. 3).

A repeatedly noted barrier to reform and experimentation in health care is the federal government and the monies it transfers to the provinces for health care. These funds are available only to those provinces who abide by the rules, regulations, and federal interpretations of the Canada Health Act.[54] The Act specifically disallows a variety of policies that are being used in other countries that provide universal health care to deliver better care at lower costs. The prohibited policies include cost sharing and extra billing.

Applying the lessons of the successful welfare reforms introduced in the mid-1990s suggests a similar opportunity for health care. The federal government should reduce CHT payments over the next two years by $6.2 billion (total) but simultaneously provide the provinces with more flexibility to experiment with different models of health care delivery within a universal and portable framework. Such an arrangement would close the deficit gap for the federal government while allowing the provinces to deal honestly with the single largest source of spending and the quickest growing area of spending in provincial budgets.[55]

Figure 29 contrasts the currently expected CHT payments for 2008/09 to 2014/15 as well as the proposed reductions. The reductions proposed are based on achieving a balanced budget within two years assuming current revenues.[56] CHT payments would be reduced by $3.1 billion in 2011/12 and an additional $3.1 billion in 2012/13, resulting in a cumulative reduction of $6.2 billion by 2012/13. Under the proposed plan presented in figure 29, the annual percentage increases in CHT payments after 2012/13 exceed the currently scheduled increases in both 2013/14 and 2014/15. These reductions coupled with those already proposed would allow for an overall balanced budget by the federal government.

In exchange for the reduction in CHT payments, the federal government would revise the Canada Health Act to require universality and portability but eliminate the other requirements of the CHA. This would afford provinces greater flexibility to experiment and innovate with different health design and delivery models within a universal and portable framework. To be absolutely clear, this proposal retains the requirement for universal coverage and portablility but allows for greater experimentation and testing of different ways in which to deliver health care services at the provincial level.

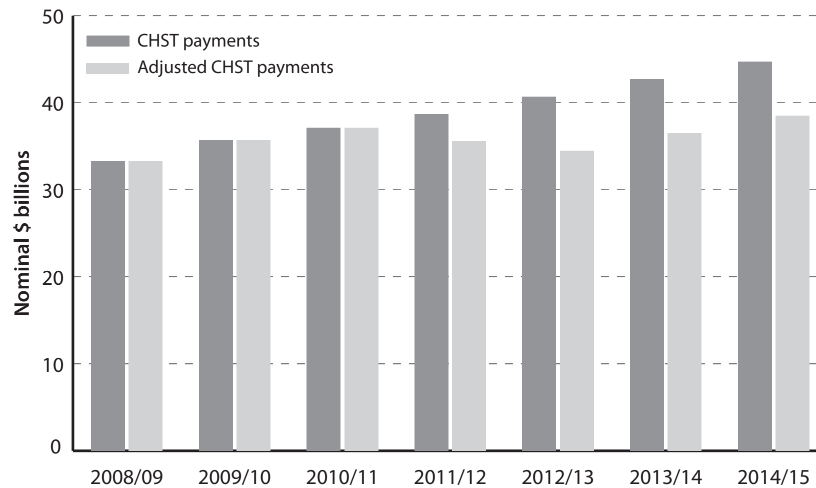
It is this experimentation and innovation that will reveal better ways to provide Canadians with health care commensurate with the resources being

54 For a detailed explanation of the Canada Health Act, see Canada, Ministry of Health, 2009; for its history, see Orchard and Alsford, 2010.

55 Under this approach roughly 29% of the reduction in program spending by 2012/13 is accomplished through the reduction in the health transfer (CHT) to the provinces.

56 Revenues are based on the most recent economic forecast (Canada, Department of Finance, 2010d).

Figure 29: Planned and adjusted CHST payments (nominal $ billions), 2008/09–2014/15



Notes: CHST = Canada Health and Social Transfer.
Sources: Canada, Department of Finance, 2010a, 2010d; calculations by authors.

provided.[57] Those reforms might include everything from insurance experimentation to the use of health savings accounts to expanded public coverage. By allowing the provinces to pursue different methods of delivery, regulation, and management of health care, we can discover, through experimentation, better and more cost-effective ways to maintain and indeed improve our nation's health care system. The key again, however, is to allow experimentation and innovation within a framework of universal coverage and access.

57 There is another interesting parallel to consider when contemplating the efficacy of the health care reforms suggested: Canada's approach to K-12 education. Canada has no federal involvement in K-12 education and the provinces are exclusively responsible for the financing, provision, and regulation of K-12 education. Not surprisingly, this has led to many different approaches to providing primary and secondary education. Interestingly, Canada spends less and achieves better results than the United States, whose system is increasingly centralized in Washington, DC. For further information on the comparison between education in the US and Canada, see Izumi and Clemens, 2010; and Izumi, Clemens, and Ou, 2010.

Conclusion

Two reforms have been proposed to eliminate the federal deficit over a two-year period. The first is to ensure that the temporary stimulus spending introduced in the 2009 budget remains temporary rather than simply becoming more permanent spending, which is the current plan. If portions of the stimulus spending are deemed priorities through a review process similar to the one used by the Liberals in 1995, then spending reductions in other areas should be identified. The second reform is to marginally reduce CHT payments to the provinces in exchange for greater flexibility and autonomy for the provinces in delivering health care, a plan based on the successful welfare reforms of the 1990s.

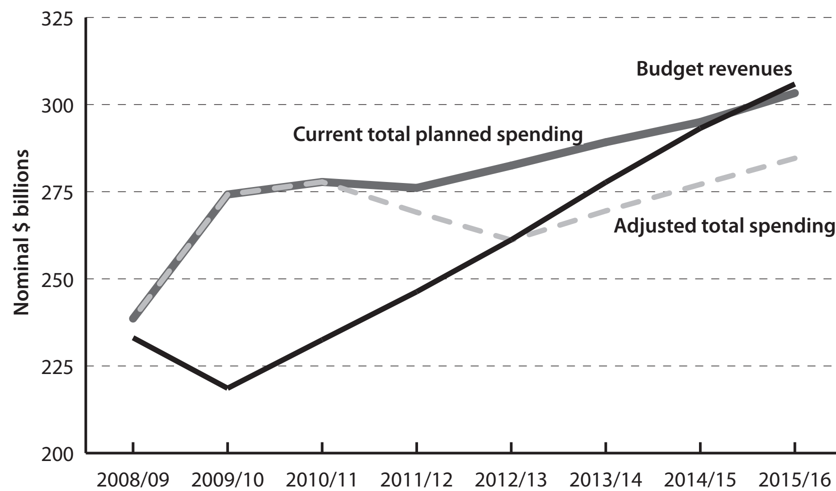
Table 5 summarizes the revised fiscal plan based on these two proposed reforms. Figure 30 illustrates the revised spending and expected revenues. Program spending is reduced by a total of $10.9 billion in 2011/12 compared to 2010/11 and by $11.0 billion in 2012/13 compared to 2011/12 (revised) through both the elimination of stimulus spending and reductions in CHT payments to the provinces. The fiscal plan contained in table 5 results in balanced budgets and small budget surpluses beginning in 2012/13. The federal government's current fiscal plan calls for the accumulation of debt through deficits of $61.6 billion between 2011/12 and 2015/16. The revised fiscal plan (table 5) actually results in a $22.9 billion cumulative surplus over the same period due to the attainment of a balanced budget much sooner than currently anticipated. The quicker return to a balanced budget means less debt accumulation and the availability of sizeable surpluses beginning in 2013/14, which allows for higher spending and/or lower taxes.[58]

Perhaps most importantly, the revised plan depicted in figure 30 and detailed in table 5 discards the failed principles of the 1980s and 1990s, which the federal government is relying on today, and builds on the successes of the reform budget of 1995. The plan calls for reduced program spending from elimination of stimulus spending coupled with moderate reductions in CHST payments rather than an attempt to slow the growth in spending while hoping for strong revenue growth over time. This latter approach failed throughout the 1980s and early 1990s, leaving Canada with a large debt and substantial interest payments. The plan offered here heeds the lessons of the reform budget of 1995, which put Canada's federal finances back on track.

58 The plan outlined in table 5 does not alter the current assumptions about debt charges, which would likely be lower given the reduced accumulation of debt.

The combination of ensuring that stimulus spending is actually temporary rather than simply more permanent spending and the reform of health care transfers and federal regulation offers an opportunity not only to balance the country's financial affairs but also to begin solving the various health care problems discussed previously.

Figure 30: Federal planned and adjusted total spending and expected budget revenues (nominal $ billions), 2008/09–2015/16



Notes: Program spending for 2008/09 is taken from the 2009 Budget, the remaining figures from the *Update of Economic and Fiscal Projections* (Canada, Department of Finance, 2010d). Debt charges for 2008/09 are taken from the 2009 Budget (Canada, Department of Finance, 2009), the remaining figures from the *Update of Economic and Fiscal Projections*. Revenue figures for 2008/09 to 2010/11 were taken from the 2010 Budget (Canada, Department of Finance, 2010a), the remaining figures are from the *Update of Economic and Fiscal Projections*.
Sources: Canada, Department of Finance, 2009, 2010a, 2010d; calculations by authors.

Table 5: Revised Federal Fiscal Plan, 2011/12 –2015/16

	Budget revenues	Current planned program spending	Debt charges	Total planned spending	Adjusted program spending*	CHST savings (revised plan)**	Adjusted program spending (balanced budget)***	Adjusted total spending	Adjusted deficit or surplus
2008/09	233.1	207.9	30.7	238.6		—	207.9	238.6	
2009/10	218.6	244.8	29.4	274.2		—	244.8	274.2	
2010/11	232.5	246.6	31.3	277.8		—	246.6	277.8	
2011/12	246.3	242.7	33.4	276.1	238.8	3.1	235.7	269.1	−22.8
2012/13	261.2	246.1	36.4	282.5	230.9	6.2	224.7	261.1	0.1
2013/14	277.7	251.7	37.5	289.2	238.2	6.2	232.0	269.5	8.2
2014/15	293.2	257.2	37.8	295.0	245.5	6.2	239.3	277.1	16.1
2015/16	305.9	265.4	37.8	303.3	253.0	6.2	246.8	284.6	21.3

Notes: Program spending for 2008/09 is taken from the 2009 Budget, the remaining figures are from the *Update of Economic and Fiscal Projections* (Canada, Department of Finance, 2010d). Debt charges for 2008/09 are taken from the 2009 Budget (Canada, Department of Finance, 2009), the remaining figures from the *Update of Economic and Fiscal Projections*. Total Planned Spending is simply the addition of planned program spending with debt charges. Revenue figures for 2008/09 to 2010/11 were taken from the 2010 Budget (Canada, Department of Finance, 2010a), the remaining figures from the *Update of Economic and Fiscal Projections*. *The Adjusted Program Spending column is calculated by taking 2008/09 pre-stimulus program spending and increasing it annually by the rate of population growth plus inflation. **The revised CHST payments and the subsequent savings are derived from figure 30. ***The Adjusted Program Spending (Balanced Budget) series is calculated using the previous Adjusted Program Spending data plus the additional CHST savings in order to achieve a balanced budget in 2012/13.

Sources: Canada, Department of Finance, 2009; 2010d; calculations by authors.

References

Alesina, Alberto, Roberto Perotti, Francesco Giavazzi, and Tryphon Kollintzas (1995). Fiscal Expansions and Fiscal Adjustment in OECD Countries. *Economic Policy* 10, 21 (October): 207–48.

Alesina, Alberto, Silvia Ardagna, Roberto Perotti, and Fabio Schiantarelli (2002). Fiscal Policy, Profits, and Investment. *American Economic Review* 92, 3: 571–89.

Barua, Bacchus, Mark Rovere, and Brett J. Skinner (2010). *Waiting Your Turn: Wait Times for Health Care in Canada: 2010 Report*. Fraser Institute. <http://www.fraserinstitute.org/uploadedFiles/fraser-ca/Content/research-news/research/publications/waiting-your-turn-2010.pdf>.

Beauchesne, Eric (1994, December 6). Reduce Debt Faster, Canada Told: Meeting Existing Target Is a Strict Minimum, OECD Warns. *Vancouver Sun*.

Boessenkool, Kenneth J. (1997). *Back to Work: Learning from the Alberta Welfare Experiment*. C.D. Howe Institute. <http://www.cdhowe.org/pdf/Kbkool.pdf>.

Canada West Foundation (1997). *Welfare Reform in Alberta: A Survey of Former Recipients*. <http://www.cwf.ca/V2/files/199713.pdf>.

Canadian Institute for Health Information (2010). *National Health Expenditure Trends, 1975–2010*. CIHI. <http://secure.cihi.ca/cihiweb/products/NHEX_Trends_Report_2010_final_ENG_web.pdf>.

Clemens, Jason, and Chris Schafer (2002). *Welfare Reform in British Columbia: A Report Card*. Fraser Institute. <http://www.fraserinstitute.org/commerce.web/product_files/WelfareReforminBC.pdf>.

Clemens, Jason, and Niels Veldhuis, eds (2007). *Beyond Equalization: Examining Fiscal Transfers in a Broader Context*. Fraser Institute

Clemens, Jason, Niels Veldhuis, and Milagros Palacios (2007). Federal Transfers and the Fiscal Balance: A Primer. *Fraser Forum* (March): 4–8. <http://www.fraserinstitute.org/uploadedFiles/fraser-ca/Content/research-news/research/articles/federal-transfers-and-the-fiscal-balance.pdf>.

Clemens, Jason, Niels Veldhuis, and Julie Kaszton (2010). *No Bang for the Taxpayer's Buck: Why California Must Reform Spending and Trim Government*. Pacific Research Institute. <http://www.pacificresearch.org/publications/no-bang-for-the-taxpayers-buck-why-california-must-reform-spending-and-trim-government>.

Crowley, Brian Lee, Jason Clemens, and Niels Veldhuis (2010). *The Canadian Century: Moving Our of America's Shadow*. Key Porter.

Elton, David (1997). *Where Are They Now? Assessing the Impact of Welfare Reform on Former Recipients, 1993–1996*. Canada West Foundation.

Emes, Joel, and Andrei Kreptul (1999). *The Adequacy of Welfare Benefits in Canada*. Fraser Institute. <http://oldfraser.lexi.net/publications/critical_issues/1999/welfare_benefits/>.

Esmail, Nadeem, and Michael Walker (2008). *How Good Is Canadian Health Care? 2008 Edition*. Fraser Institute. <http://www.fraserinstitute.org/commerce.web/product_files/HowGoodisCanadianHealthCare2008.pdf>.

Finnie, Ross, and Ian Irvine (2008). *The Welfare Enigma: Explaining the Dramatic Decline in Canadians' Use of Social Assistance, 1993–2005*. C.D. Howe Institute. <http://www.cdhowe.org/pdf/commentary_267.pdf>.

Finnie, Ross, Ian Irvine and Roger Sceviour (2005). *Social Assistance Use in Canada: National and Provincial Trends in Incidence, Entry and Exit.* Analytical Studies Research Paper no. 245 (May). Catalogue no. F0019M1E. Statistics Canada. <http://www.statcan.gc.ca/pub/11f0019m/11f0019m2005246-eng.pdf>.

Gabel, Todd, Jason Clemens, Sylvia LeRoy, and Niels Veldhuis (2003). Staying the Course on Welfare Time Limits. *Fraser Forum* (December). Fraser Institute. <http://www.fraserinstitute.org/commerce.web/product_files/FraserForum_December2003.pdf>.

International Monetary Fund (2008). Fiscal Policy as a Countercyclical Tool. In *World Economic Outlook*, October 2008 (IMF): 159–96. <http://www.imf.org/external/pubs/ft/weo/2008/02/pdf/c5.pdf>.

Izumi, Lance, and Jason Clemens (2010, February 23). Learning from Canada's Schools. *Washington Times*: <http://www.washingtontimes.com/news/2010/feb/23/learning-from-canadas-schools>.

Izumi, Lance, Jason Clemens, and Lingxiao Ou (2010, July 2). What Canada Can Teach the U.S. about Education. *National Post*. Available at <http://www.pacificresearch.org/press/what-canada-can-teach-the-us-about-education>.

Karabegović, Amela, Charles Lammam, and Niels Veldhuis (2010). Did Government Stimulus Fuel Economic Growth in Canada? An Analysis of Statistics Canada Data. Fraser Institute. <http://www.fraserinstitute.org/research-news/display.aspx?id=15912>.

Kotlikoff, Lawrence J., and Christian Hagist (2005). *Who's Going Broke? Comparing Healthcare Costs in Ten OECD Countries*. NBER Working Paper 11833. National Bureau of Economic Research.

Lammam, Charles, and Niels Veldhuis (2010). Ignatieff Has It Backward on Corporate Income Taxes. *Fraser Forum* (November/December): 33–34. <http://www.fraserinstitute.org/research-news/research/display.aspx?id=16923>.

Martin, Paul (2008) *Hell or High Water: My Life In and Out of Politics*. McClelland & Stewart.

Mark Milke (2008). *Corporate Welfare: Now a $182 Billion Addiction. A Fiscal Update on Business Subsidies in Canada*. Fraser Alert (December). Fraser Institute. <http://www.fraserinstitute.org/research-news/display.aspx?id=12945>.

Milke, Mark (2009). *Canada's Corporate Welfare Bill: $30,252 per Family. The Justifications for Corporate Welfare Fail Again*. Frontier Centre for Public Policy. <http://www.fcpp.org/publication.php/3067>.

Murphy, Robert P., and Jason Clemens (2010). *Taxifornia: California's tax system, comparisons with other states, and the path to reform in the Golden State*. Pacific Research Institute. <http://www.pacificresearch.org/publications/taxifornia>.

Orchard, Beatrice A., and Stephen Alsford (2010). Making Medicare: The History of Health Care in Canada, 1914–2007. Canadian Museum of Civilization. <http://www.civilization.ca/cmc/exhibitions/hist/medicare/medic00e.shtml>.

Palacios, Milagros, and Kumi Harischandra (2008). The Impact of Taxes on Economic Behavior. In Jason Clemens (ed), *The Impact and Cost of Taxation in Canada: The Case for Flat Tax Reform* (Fraser Institute): 3–31.

Palacios, Milagros, Niels Veldhuis, and Kumi Harischandra (2008). *Canadian Government Debt 2008: A Guide to the Indebtedness of Canada and the Provinces*. Fraser Institute. <http://www.fraserinstitute.org/research-news/display.aspx?id=12881>.

Reinhart, Carmen M., and Kenneth S. Rogoff (2009). *This Time Is Different: Eight Centuries of Financial Folly*. Princeton University Press.

Richards, John (1997). *Retooling the Welfare State: What's Right, What's Wrong, What's To Be Done*. C.D. Howe Institute.

Richards, John (2000). *Now That the Coat Fits the Cloth...* . Commentary No. 143 (June). CD Howe Institute. <http://www.cdhowe.org/pdf/rich-4.pdf>.

Rovere, Mark, and Brett J. Skinner (2010). *Value for Money from Health Insurance Systems in Canada and the OECD*. Fraser Institute. <http://www.fraserinstitute.org/uploadedFiles/fraser-ca/Content/research-news/research/publications/value-for-money-health-insurance-systems.pdf>.

Sabatini, E. (Rico) (1996). *Welfare—No Fair: A Critical Analysis of Ontario's Welfare System (1985–1994)*. Fraser Institute.

Santayana, George (1905/1980). *Reason in Common Sense. The Life of Reason*, Vol. 1. Dover. Available at <http://www.gutenberg.org/files/15000/15000-h/vol1.html>.

Savoie, Donald J. (1999). *Governing from the Centre: The Concentration of Power in Canadian Politics*. University of Toronto Press.

Schafer, Chris, Joel Emes, and Jason Clemens (2001). *Surveying US and Canadian Welfare Reform*. Fraser Institute. <http://www.fraserinstitute.org/research-news/display.aspx?id=13457>.

Taylor, John B. (2011, January 14). Higher Investment Best Way to Reduce Unemployment, Recent Experience Shows. *Economics One: A Blog by John B. Taylor*. <http://johnbtaylorsblog.blogspot.com/2011/01/higher-investment-best-way-to-reduce.html>.

TD Economics (2009). *A Primer on Fiscal Stimulus*. <http://www.td.com/economics/special/jm0209_stimulus.pdf>.

The Economist (2003, September 25). Canada's New Spirit. <http://www.economist.com>.

Veldhuis, Niels, and Jason Clemens (2003). Clarifying the Federal Government's Contribution to Health Care. *Fraser Forum* (February): 3–5. <http://www.fraserinstitute.org/research-news/research/display.aspx?id=13034>.

Wall Street Journal (1995, January 12). Canada Bankrupt? Editorial.

Government sources

Canada, Department of Finance (1984). *The Fiscal Plan*.

Canada, Department of Finance (1985). *The Fiscal Plan*.

Canada, Department of Finance (1986). *The Fiscal Plan*.

Canada, Department of Finance (1987). *The Fiscal Plan*.

Canada, Department of Finance (1994). *Budget Plan 1994*.

Canada, Department of Finance (1995a). *Budget 1995: Facts Sheets. The Canada Social Transfer*. <http://www.fin.gc.ca/budget95/fact/FACT_10-eng.asp>.

Canada, Department of Finance (1995b). *Budget in Brief*. <http://www.fin.gc.ca/budget95/binb/brief.pdf>.

Canada, Department of Finance (1996). *Budget in Brief*. <http://www.fin.gc.ca/budget96/binb/brief.pdf>.

Canada, Department of Finance (2000). *Budget Plan 2000: Better Finances, Better Lives*. <http://www.fin.gc.ca/budget00/pdf/bpe.pdf>.

Canada, Department of Finance (2008). *Budget 2008: Responsible Leadership*. <http://www.budget.gc.ca/2008/home-accueil-eng.html>.

Canada, Department of Finance (2009). *Canada's Economic Action Plan: Budget 2009*. <http://www.budget.gc.ca/2009/pdf/budget-planbugetaire-eng.pdf>.

Canada, Department of Finance (2010a). *Budget 2010: Leading the Way on Jobs and Growth*. <http://www.budget.gc.ca/2010/pdf/budget-planbudgetaire-eng.pdf>.

Canada, Department of Finance (2010b). *Canada's Economic Action Plan: A Sixth Report to Canadians* (September). <http://www.fin.gc.ca/pub/report-rapport/2010-09-27/index-eng.asp>.

Canada, Department of Finance (2010c). *Fiscal Reference Tables*. (October) <http://www.fin.gc.ca/frt-trf/2010/frt-trf-10-eng.asp>.

Canada, Department of Finance (2010d). *Update of Economic and Fiscal Projections, October 2010*. <http://www.fin.gc.ca/ec2010/efp-pef-eng.asp>.

Canada, Ministry of Health (2008). *Healthy Canadians: A Federal Report on Comparable Health Indicators*. Ministry of Health. <http://www.hc-sc.gc.ca/hcs-sss/alt_formats/hpb-dgps/pdf/pubs/system-regime/2008-fed-comp-indicat/index-eng.pdf>.

Canada, Ministry of Health (2009). *Canada Health Act – Annual Report 2008-09*. Ministry of Health. <http://www.hc-sc.gc.ca/hcs-sss/alt_formats/pdf/pubs/cha-ics/2209-cha-ics-ar-ra/chaar-ralcs-09-eng.pdf>.

Canada, Receiver General For Canada (2010). *Public Accounts of Canada 2010*. <http://www.tpsgc-pwgsc.gc.ca/recgen/txt/72-eng.html>.

Martin, Paul (1994). *The Budget Speech*. February 22. Department of Finance Canada.

Martin, Paul (1995). *Budget Speech*. February 27. Department of Finance Canada.

Roy, F. (2004). *Social Assistance by Province, 1993–2003*. *Canadian Economic Observer* (November): 3.1–3.7. Statistics Canada catalogue no. 11-010-XIB. <http://www.statcan.gc.ca/pub/11-010-x/11-010-x2004011-eng.pdf>.

Statistics Canada (2010a). *Consumer Price Index (CPI), 2005 basket, annual*. CANSIM table 326-0021. <http://www.statcan.gc.ca>.

Statistics Canada (2010b). Financial market statistics (last Wednesday unless otherwise stated, monthly). <http://cansim2.statcan.gc.ca/cgi-win/cnsmcgi.exe?Lang=E&RootDir=CII/&ResultTemplate=CII/CII___&Array_Pick=1&ArrayId=1760043>.

Statistics Canada (2010c). *Estimates of population, by age and sex for July 1, Canada, provinces and territories, annual*. CANSIM table 051-0001. <http://www.statcan.gc.ca>.

Statistics Canada (2010d). *Federal, provincial and territorial general government revenue and expenditures, for fiscal year ending March 31*. CANSIM Table 385-0002. <http://www.statcan.gc.ca>.

Statistics Canada (2010e). *Provincial Economic Accounts: Data Tables.* <http://www.statcan.gc.ca/pub/13-018-x/13-018-x2010001-eng.htm>.

United States, Congressional Budget Office [US-CBO] (2010). *Long Term Budget Outlook (June).* <http://cbo.gov/doc.cfm?index=11579>.

About the authors

Jason Clemens

Jason Clemens is the Director of Research at the Pacific Research Institute and a senior fellow of the Fraser Instiute. Prior to joining PRI, he held a number of positions at the Canadian-based Fraser Institute over a ten-plus year period, including the director of research quality, resident scholar in fiscal studies, and the director of strategic planning and budgeting. He has an honors B.A. in Commerce and an M.A. in Business Administration from the University of Windsor as well as a post-baccalaureate degree in Economics from Simon Fraser University.

Mr Clemens has published over 50 major studies on a wide range of topics, including taxation, government spending, labor market regulation, banking, welfare reform, productivity, entrepreneurship, public choice economics, and economic prosperity. He has published over 250 shorter articles, which have appeared in such newspapers as the *Wall Street Journal*, *Investors Business Daily*, *National Post*, *Globe & Mail*, and all major daily papers in Canada. His articles have also been published in major US papers and websites such as the *Washington Post*, *L.A. Daily News*, *San Francisco Chronicle*, *San Diego Union-Tribune*, *Baltimore Sun*, *Detroit Free Press* and *Detroit News*, *Pittsburgh Tribune-Review*, *Sacramento Bee*, *Human Events*, *Townhall.com*, and *Flash Report*. Mr Clemens has been a guest on numerous radio and television programs across Canada and the United States, including *ABC News*. He has appeared before committees of both the House of Commons and the Senate in Canada as an expert witness and testified before state legislatures in California. In 2006, he received the prestigious Canada's *Top 40 Under 40* award presented by Caldwell Partners as well as an *Odyssey Award* from the University of Windsor.

Milagros Palacios

Milagros Palacios is a senior research economist in the Fiscal Studies Department at the Fraser Institute. She holds a B.A. in Industrial Engineering from the Pontifical Catholic University of Peru and an M.Sc. in Economics from the University of Concepción, Chile. She is co-author of *Measuring the Fiscal Performance of Canada's Premiers, Measuring Labour Markets in Canada and the United States, Fiscal Performance Index, Tax Freedom Day, Canadian Provincial Investment Climate Report, An Empirical Comparison of Labour Relations Laws in Canada and the United States, Union Disclosure in Canada and the United States, Canadian Government Debt,* and

Transparency of Labour Relations Boards in Canada and the United States. Her recent commentaries have appeared in such newspapers as the *National Post* and *Windsor Star*. Since joining the Institute, Ms Palacios has written regularly for *Fraser Forum* on a wide range of topics, including labour regulation, fiscal issues, taxation, charitable giving, and a host of environmental issues such as air quality, Kyoto, and water transfers.

Niels Veldhuis

Niels Veldhuis is Vice President Research at the Fraser Institute. As an economist, Niels has written five books and over 50 comprehensive studies on a wide range of economic topics including, taxes, banking, entrepreneurship, and government finances. He has written over 200 articles, which have appeared in over 50 newspapers including the *Globe and Mail* and *Wall Street Journal*. Niels currently writes a bi-weekly column for the *Financial Post*. He appears regularly on radio and television programs across the country and has appeared before committees of both the House of Commons and the Senate as an expert witness. His latest book, *The Canadian Century: Moving Out of America's Shadow*, was published by Key Porter in May 2010. Niels holds a Bachelor's degree in Business Administration, with joint majors in business and economics and a Master's Degree in Economics from Simon Fraser University. In 2011, Niels was named one of Vancouver's Top 40 under 40 by *Business in Vancouver*.

Acknowledgments

The authors would like to thank the Fraser Institute supporters who generously provided the resources for us to undertake this study. A special thanks to the Barbara and Bob Mitchell Fund for its generous support. In addition, we are grateful for the comments and suggestions provided by two anonymous peer-reviewers.

Any errors, omissions, or mistakes remain the sole responsibility of the authors. As the authors have worked independently, the views and analysis expressed in this document remain those of the authors and do not necessarily represent the views of the supporters, trustees, or other staff at the Fraser Institute.

Publishing information

Periodically, the Fraser Institute publishes timely and comprehensive studies of current issues in economics and public policy. This study is one such example belonging to a series of related publications.

Distribution

These publications are available from <http://www.fraserinstitute.org> and <http://www.fraseramerica.org> in Portable Document Format (PDF) and can be read with Adobe Acrobat® 7 or later or with Adobe Reader® 7 or later. Adobe Reader® X, the most recent version, is available free of charge from Adobe Systems Inc. and may be down-loaded from: <http://get.adobe.com/reader/>. We encourage you to install the most recent version.

Ordering publications

For information about ordering the printed publications of the Fraser Institute, please contact the publications coordinator

- e-mail: sales@fraserinstitute.org
- telephone: 604.688.0221 ext. 580 or, toll free, 1.800.665.3558 ext. 580
- fax: 604.688.8539.

Media

For media inquiries, please contact our Communications Department

- 604.714.4582
- e-mail: communications@fraserinstitute.org.

Disclaimer

The authors of this publication have worked independently and opinions expressed by them are, therefore, their own, and do not necessarily reflect the opinions of the supporters, trustees, or other staff of the Fraser Institute. This publication in no way implies that the Fraser Institute, its trustees, or staff are in favor of, or oppose the passage of, any bill; or that they support or oppose any particular political party or candidate.

Copyright

Copyright© 2011 by the Fraser Institute. All rights reserved. No part of this publication may be reproduced in any manner whatsoever without written permission except in the case of brief passages quoted in critical articles and reviews.

ISSN

ISSN 1923-371X Studies in Budget and Tax Policy (print version)
ISSN 1923-3728 Studies in Budget and Tax Policy (online version)

Date of issue

February 2011

Citation

Veldhuis, Niels, Jason Clemens, and Milagros Palacios (2011). *Budget Blueprint: How Lessons from Canada's 1995 Budget Can Be Applied Today*. Fraser Institute

Editing and design

Lindsey Thomas Martin.

Cover design

Bill Ray

Images for cover

Man with laptop © Elenathewise; Fotolia
Pressione fiscale © Comugnero Silvana; Fotolia
Economy cut © Giordano Aita; Fotolia
Filing Taxes Receipts © redrex; Fotolia
Stack of Folders © Lai Leng Yiap;Bigstock
Scales on white, © Iserg; Birstock.

Supporting the Fraser Institute

To learn how to support the Fraser Institute, please contact

- Development Department, Fraser Institute
  Fourth Floor, 1770 Burrard Street
  Vancouver, British Columbia, V6J 3G7 Canada
- telephone, toll-free: 1.800.665.3558 ext. 586
- e-mail: development@fraserinstitute.org.

About the Fraser Institute

Our vision is a free and prosperous world where individuals benefit from greater choice, competitive markets, and personal responsibility. Our mission is to measure, study, and communicate the impact of competitive markets and government interventions on the welfare of individuals. Founded in 1974, we are an independent Canadian research and educational organization with locations throughout North America and international partners in over 70 countries. Our work is financed by tax-deductible contributions from thousands of individuals, organizations, and foundations. In order to protect its independence, the Institute does not accept grants from government or contracts for research.

Nous envisageons un monde libre et prospère, où chaque personne bénéficie d'un plus grand choix, de marchés concurrentiels et de responsabilités individuelles. Notre mission consiste à mesurer, à étudier et à communiquer l'effet des marchés concurrentiels et des interventions gouvernementales sur le bien-être des individus.

Nuestra visión es un mundo libre y próspero donde los individuos se beneficien de una mayor oferta, la competencia en los mercados y la responsabilidad individual. Nuestra misión es medir, estudiar y comunicar el impacto de la competencia en los mercados y la intervención gubernamental en el bienestar de los individuos.

Editorial Advisory Board

Prof. Armen Alchian

Prof. Terry Anderson

Prof. Robert Barro

Prof. Michael Bliss

Prof. James M. Buchanan†

Prof. Jean-Pierre Centi

Prof. John Chant

Prof. Bev Dahlby

Prof. Erwin Diewert

Prof. Stephen Easton

Prof. J.C. Herbert Emery

Prof. Jack L. Granatstein

Prof. Herbert G. Grubel

Prof. Friedrich A. Hayek* †

Prof. James Gwartney

Prof. H.G. Johnson*

Prof. Ronald W. Jones

Dr. Jerry Jordan

Prof. Ross McKitrick

Prof. Michael Parkin

Prof. F.G. Pennance*

Prof. Friedrich Schneider

Prof. L.B. Smith

Prof. George Stigler* †

Mr. Vito Tanzi

Sir Alan Walters

Prof. Edwin G. West*

* deceased
† Nobel Laureate