

## Faculty Commentary

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Dear Premier-designate Ford,

Congratulations on your majority win in the June 7<sup>th</sup> election.

Your acceptance speech was inspiring. Improving the well-being of Ontarians and making the Ontario economy a tower of strength are aspirations everyone can get behind.

Now you face the daunting task of leading the Province to secure these objectives in the context of the numerous challenges you and your Party have inherited.

### **Fiscal Situation**

You have wisely identified addressing Ontario's fiscal disorder as your Government's first priority. You will need to assess the fiscal situation of the Ontario Government and evaluate what that will mean for the plans you laid out during the election campaign.

The fiscal picture is not pretty.

The Liberals were crawling out of their large deficits, only to propose plunging the province back into a sea of red ink. But even without implementing any of the Liberal's proposals since the reasonably responsible 2017 budget - initiatives that add up to about \$6 billion a year - the fiscal books would still be out of balance. A chief concern is the 37 per cent net debt-to-GDP ratio. This compares to 26 per cent prior to the financial crisis and recession. It is even above the debt burden of the 1990s when the Conservative Government of the day accepted that Ontario was in fiscal crisis and took strong action. Left to anything resembling the status quo, there will be large deficits over a protracted period and the debt burden will rise further.

This would of course be unacceptable to everybody, including your Government.

Almost immediately you will need to resolve what the Liberals derisively described as a disagreement among accountants over electricity and civil service pension funds. You will no doubt be getting a detailed briefing on this dispute. Let me cut to the bottom line. The Auditor General is right and the Liberals wrong. Adopting the

accounting conventions recommended by the Auditor General adds about \$6 billion per year to projected deficits, an unwelcome but necessary addition.

Your election platform is to balance the budget “on a responsible timeframe”. This is a softer position than the references earlier in the campaign to balance the budget before the end of the mandate.

When you sit down with officials from the Ministry of Finance you will realize that the fiscal situation you inherited is going in the wrong direction from both the earlier and final timeframes set for balancing the budget. And that is even before accommodating the many initiatives contained in the campaign plans to increase spending and cut taxes.

Even at that, you should be wary of the numbers the Finance officials come bearing. Those projections will likely be based on the assumption of future real economic growth in Ontario of around 2 per cent per annum. Yet if the record of productivity growth in Ontario since 2000 continues, growth is likely to be only around 1 ½ per cent per annum. Of course your objective to strengthen Ontario’s economy is essentially a pledge to raise that productivity growth rate. But unless or until that is achieved, fiscal limits abound. The mathematics of knocking ½ percentage points off accumulating growth rates does terrible things to projections of the revenues available to support the provision of programs and services.

Further, due to the many headwinds facing the economy, there is no guarantee of hitting an average or sustainable economic growth rate over the next several years. Perhaps the most powerful concern is what lies ahead for trading relations with the United States given that trade with our southern neighbor is a central feature of the Ontario economy.

### **Spending Cuts from Rooting Out Inefficiency**

During the election campaign your party referred to cutting overall program spending by 4 per cent a year, or around \$6 billion, through cutting inefficient programs and services. Balancing the budget with this savings will be difficult enough; impossible without.

Having spent a year conducting exactly such an exercise in 2011-12 as Chair of the Commission on the Reform of Public Services, I can offer some insights into this initiative. First, the good news. It can be done. An intensive examination of how Ontario spends tax payers’ money reveals that a lot of things can be done more effectively and more efficiently. However, from my experience I would advise that the effort will be frustrating and ultimately futile under the expectations and conditions discussed during the election campaign.

Unfortunately, there are not billions of dollars dangling at the end of tree branches that can be plucked without affecting anything or anyone. Every dollar Ontario spends goes to someone for something. The recipients of that dollar and the people delivering the program or service will be affected.

To address this, the initiative needs to be rounded out to embrace a further condition. The end result of the review should not just be greater efficiency and cost savings. The effectiveness of spending should also be elevated. This is key to enhancing the well-being of Ontarians and strengthening the economy. It changes a spending review from being a bean-counting exercise to being at the heart of delivering services in better ways.

The second revision to the planned spending review is to amend the condition that no civil service jobs will be affected. For many programs the labour bill is a large portion of the total cost so it is difficult to secure savings without affecting civil service jobs. Further, if workers in inefficient areas are transferred elsewhere the efficiency of those other areas will be negatively affected because the additional workforce may not be needed there. Relying on attrition or hiring freezes has never worked because it takes too long to accumulate savings and workers usually leave from areas where they are needed as opposed to the areas targeted for their inefficiency.

None of this advice is intended to deter you from launching immediately a review of where savings can be secured. It is rather to point out that the exercise will be difficult and success requires addressing multiple goals, including not just driving up efficiency and securing savings but simultaneously improving the effectiveness of programs and services in hitting economic and social goals.

### **Campaign Initiatives**

Once you have gone through the exploration of the accounting, economic and fiscal situations, you will find it will be extremely difficult if not impossible to reconcile all the elements of the election platform. More specifically, all the spending initiatives and the proposed tax cuts cannot be accommodated within the provision of balancing the budget over a “responsible timeframe”. And about the last thing you will want to do is repeat the error of many previous governments of setting out a plan on a wish and a prayer and then constantly miss targets. The loss of credibility is deadly.

A second look will be in order for many of the campaign pledges to ensure they fit with the economic and fiscal situations you and your Government inherited. In some areas such a review could be very fruitful. I will offer but a few examples.

### **Health**

Healthcare is by far the biggest spending ticket in the Ontario Budget, creeping up on half of program spending. The election platform proposed spending yet more. But the proposed spending increases may be in the wrong areas. Instead, a focus on the right areas could yield both lower spending and improvements in health and healthcare. As an example, much was made of “hallway” medicine during the election campaign. The instinct is to add greater hospital capacity. Yet at any given time, more than 10 per cent of the people in hospitals should not be in those facilities. Their needs could and should be met elsewhere both at much lower cost and greater satisfaction to them and their families.

The focus should be on well coordinated social combined with health care delivered in people’s homes and communities - all places people would rather be as opposed to hospitals or long-term care facilities.

Further, before committing to new money for new initiatives, stock must be taken of what award emerges from the arbitration process playing out at this moment with the Ontario Medical Association. An award exceeding what is embedded in fiscal plans could not only soak up all the money set aside for new initiatives, but could become a beacon for pressure from other public sector wage negotiations.

### **Electricity**

High and rising electricity prices is a major source of angst among Ontarians and a crippling competitiveness blow for the province’s businesses. The pressure to do “something” is intense. Yet there are no simple solutions.

The price situation has precious little to do with the partial privatization of Ontario Hydro or the compensation of its executives and Board. The issue is that your Government has inherited a situation where an excess supply of very expensive electricity is locked in through long-term contracts; contracts that in many cases are with prices that are indexed to rise further.

Scrapping or unilaterally amending contracts would be difficult legally and carry all kinds of negative implications for selling the position that “Ontario is open for business”. Cutting prices and piling the shortfalls onto public debt – in brief, the Liberal’s latest plan – is patently unfair to younger Ontarians who will already have to wrestle with the mountain of debt they are inheriting. The freight for electricity could be shifted to other tax sources, most likely the personal income tax. But that too would be unfair because it could saddle people who are not big consumers of electricity. Further, it comprises the laudable campaign pledge of lower personal income taxes.

The bottom line is that Ontarians are going to face the inherited problem of high electricity prices for some time. Some good, plain language from the new Government is in order to explain this reality.

### **Energy Taxation**

The Conservative Government is committed to scrapping Ontario's cap-and-trade system dealing with greenhouse gas emissions and to lowering the provincial gasoline excise tax. The latter will be a significant blow to the goal of balancing the budget. The former faces some tricky obstacles. Further, it would also be a blow to fiscal balance if the initiatives that the Liberals proposed to be funded from the \$2 billion of annual revenue from the auction of permits are also not scrapped. Second, there is the thorny issue of the roughly \$3 billion of permits that Canadian companies and investors already hold. Much of this is financially backed by Ontario-based banks. It is unlikely California and Quebec, the partners in the cap-and-trade arrangement, would buy these permits back at their full value. Dumping them would sink the markets in these other jurisdictions and cause huge losses in Ontario. The Government may well need to provide compensation. There was an allowance for exactly this in Patrick Brown's proposal to switch Ontario from cap-and-trade to a carbon tax.

Finally, scrapping an Ontario cap-and-trade system may just leave Ontarians with a federally-imposed carbon tax of \$50 a tonne and rising. That is, unless Saskatchewan, perhaps joined by Ontario, wins the legal battle over the constitutional line splitting federal and provincial jurisdiction. The new Government will undoubtedly be receiving legal advice that the provincial case is far from assured.

### **Other Initiatives**

Only a few major initiatives from the Conservatives election plans have been touched upon here. There are many more that would raise spending or reduce revenues. When they are laid upon a realistic depiction of the underlying economic and fiscal situation and prospects, it will become readily apparent, and quite soon, that all the pledges are not compatible. In particular, the net result of promised new initiatives would not only fail to reduce provincial deficits and address the large debt burden, they would most likely move the province further away from fiscal sustainability. In turn, an unsustainable fiscal situation would be a major drag on economic growth. The fiscal hangover inherited by this new Government is an albatross that must be removed in order to secure the important objectives that have been set out. This will require evaluating all proposed initiatives in light of the economic and fiscal challenges.

The goals of improving the well-being of Ontarians and strengthening the provincial economy are spot on. A lot of hard work lies ahead to achieve them. In some cases plans will need to be amended to fit the circumstances your Government has inherited. The Government's pledge of transparency and direct, plain talk explaining the situation and plans will be instrumental to success.

I am sure all Ontarians wish the Conservative Government of Ontario success in their pursuit of enhancing the well-being of the province's residents.

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