FOCUS ON FINANCE 2

A LOOK INTO ONTARIO'S FINANCES

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INTRODUCTION

Last year I wrote Focus on Finance, with the hope it would ring the alarm bell in Ontario to draw attention that all is not right with our finances.

Since that time many individuals, associations, rating agencies, and members of the media have weighed in – all ringing the same alarm bell.

Just reading this page alone will give you an idea of what is happening with Ontario's finances. Drafting the News Releases for each of these issues provided me with the impetus to write Focus on Finance 2.

Since last year, Moody's debt rating agency changed its outlook from "stable" to "negative", expressing their concerns over the government's ability to eliminate the deficit in 3 years. They stated, "Ontario's persistently large deficits, and its tendency to delay the most significant cost cutting measures towards the latter years of its projected timeline for returning to a balanced budget, increase the risk that the province will be unable to achieve its goal".

The Conference Board of Canada said Ontario can't meet its pledge to balance the books by 2017/18 without spending cuts or tax hikes.

The Auditor General said "Ontario's debt continues to grow faster than the province's economy, which could have negative implications for the province's finances". She concluded the consequences of high debt include "the 'crowding out' of other spending, greater vulnerability to a rise in interest rates, and a possible downgrading of the province's credit rating which would lead to higher future borrowing cost".

The Ontario Chamber of Commerce titled their report on Ontario's debt and deficit *How Bad Is It?* It opens with "Some experts are calling it a crisis and think that the Government of Ontario should be taking every step possible to balance its books". It also states, "Ontario's fiscal situation is becoming increasingly dire … we are likely to reach a state of crisis unless the province cuts spending and changes the ways it does business".

The Fraser Institute's study, *Ontario's Debt Balloon*, calculates that 66 per cent of the increase in debt since the 2008 recession is directly attributable to day-to-day expenses exceeding revenues on an annual basis. It states, "Ontario's debt has grown by $117 billion since the recession, largely because of government borrowing to fund day-to-day expenses – not investments in infrastructure".

Jamison Steeve, of the Institute for Prosperity and Competitiveness and the Martin Prosperity Institute at University of Toronto, penned a Toronto Star column *Ontario Needs Major Shift to Get Economy on Track*. In it he states, "Ontario's economy is not producing as much wealth as planned, hoped, or expected. It is time for Ontario to take a new course to grow the economy".

The Canadian Federation of Independent Business declared "Ninety-seven per cent of small businesses are concerned about the state of Ontario's economy, with 67 per cent very concerned". In addition, 91 per cent of small businesses want to see the provincial budget balanced by 2017/18.

Last summer, I thought the most alarming, and disappointing revelation came during the reading of the Fall Economic Statement. Charles Sousa, Ontario's Finance Minister, confessed that revenue would be down $500 million from his budget forecast – of only 4 months earlier! How can we trust a word this government says, when they were half-a-billion dollars off, in only 4 months?

Then, something even more alarming appeared in an answer to a routine 'Order Paper' question I posed. I asked for a line-by-line accounting of how the Ministry will balance the budget by 2017/18. I have been asking for this, because every document from the Liberal government simply shows a Revenue total, Expense total, and magically balances in 2017/18, without showing any of the 'guts' of the charts. This response came the same as all the others; no guts, just totals. But it was the wording that was alarming.

For the last couple of years, the government had been going to great pains to stress it is "on track" to balance the province's books by 2017/18. But in the Order Paper answer, they stated they were "committed" to balancing by 2017/18. That's a far less certain statement, and similar to the "aspirational" term the Premier was using last year, but quickly retreated from. The shift in language suggests there's a whole lot of hoping and wishing going on, and not a lot of evidence to back it up.

After all, as you will read in the coming pages, when I was our lead on the Gas Plant Scandal hearings, we were able to obtain 'Confidential Advice to Cabinet' documents that revealed the government is "not on track to meet deficit targets".

That's it, simply put, from Premier Kathleen Wynne's own Ministry of Finance documents. They are NOT on track to balance.

BUDGET 2015 UPDATE

Just as this book was going to press, the Finance Minister announced the deficit for Ontario will come in at $10.9 billion. He announced this as great news for Ontario, because the deficit was forecast to be $12.5 billion. Now before you join the fanfare, there are two facts you need to review. First, the deficit in 2013 was $9.2 billion, it grew to $10.5 billion last year, and has grown to $10.9 billion this year – we're going the wrong way – there's nothing to celebrate here! Secondly, as the chart on page 15 illustrates, two years ago the announced deficit was actually forecast at $10.5 billion – $400 million lower! But last year, the government fluffed up the forecast to $12.5 billion so they could announce they beat their estimate, rather than be forced to announce that they had failed miserably.

This is the kind of slight-of-hand the government uses when it comes to reporting numbers.

This is another reason why I wrote this book – Focus on Finance presents the government's own insider documents to give you a real look into Ontario's finances.

PREFACE

This morning more than 500,000 men and women in Ontario woke up without a job. Caterpillar. Wrigley's. Heinz. These are all companies that announced they're shutting their Ontario operations and heading for greener pastures. Oh, they're still making, earth moving equipment, chewing gum, and ketchup. They're just not making them in Ontario anymore.

With Ontario boasting amongst the highest energy prices in North America, the highest payroll taxes in Canada, over 8 years with unemployment higher than the national average, and a government about to institute a carbon tax and a pension tax, is it any wonder companies are abandoning Ontario in record numbers? There were 2,700 fewer small businesses in Ontario last year compared to the year before. In addition, other companies are bypassing Ontario as they search for a place to set up shop.

What happened to this once-powerful province; the envy of all Canada?

Ontario, once the economic engine of Confederation, has become a 'have-not' province, now relying on $3 billion in annual equalization payments from the federal Government. Jason Kirby of Maclean's magazine, called the government's strategy "a hodgepodge of hope, pray, and blame Ottawa." In fact, according to the Globe and Mail's Bill Curry, Ontario will get an additional $1.25 billion in transfer payments this year, bringing their total to $20.4 billion: the most of any province. Before this Liberal Government took office in Ontario, we had a low debt-to-GDP ratio. Low unemployment. Cheap hydro. Less red tape. But look at what's happened over the past decade.

Skyrocketing energy rates. New taxes. Crushing red tape. A job-killing trifecta!

Families open their hydro bills to find they are now paying amongst the highest electricity prices in North America. Businesses, which in the past set up shop in Ontario for our cheap hydro, are leaving in record numbers. Hydro rates have more than tripled in 11 years and last year the government told us they will increase a further 42 per cent by 2018.

Corporate taxes, which were scheduled to fall from 11.5 per cent to 10 per cent in the 2012 budget, were left at 11.5 per cent, as part of the Liberal's budget deal with the NDP, to win their support. In the 2014 budget , an aviation fuel tax was introduced, costing the industry $100 million. This is being passed on to customers – at least those who choose not to cross the border and fly lower-cost U.S. airlines. Now, the government has announced plans to institute a carbon tax and pension tax. Ontario employers and employees already pay the highest payroll taxes in Canada. When you add the Workplace Safety and Insurance Board tax and others, a clear tax-and-spend picture forms.

The Canadian Federation of Independent Businesses held a Red Tape Awareness Week, and disclosed that burdensome red tape costs Canadian businesses a whopping $31 billion annually. That's money that can't be re-invested in their businesses as it is used for non value-added activity, as one presenter to the Legislature's pre-budget consultations called it.

As stated earlier, skyrocketing energy rates, new taxes, and crushing red tape form the perfect storm to kill jobs in Ontario. And it's unfolding in front of us right now.

As a 2-term MPP, I've had a front-row seat from which to witness the financial crisis created by this government. My roles, first as Energy Critic, and now as Finance Critic for the PC Party of Ontario, have given me a unique opportunity to uncover what is happening to Ontario.

These pages share what I've discovered.

The first section of the book, The State of Ontario, delves into what the Liberals did to more than triple Ontario's hydro rates in 11 years. It also reveals some little-known facts about new taxes in Ontario. The section ends with a discussion on how red tape is stifling families and business.

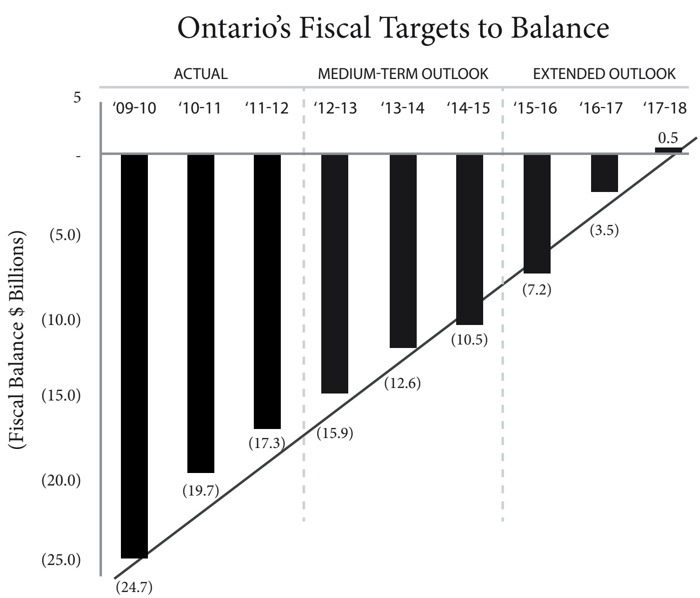
The second section, in fact the majority of the book, deals with Ontario's debt and deficit. Through the Gas Plant Scandal hearings and within the Standing Committee on Estimates, we've accessed tens of thousands of internal documents from the Ministry of Finance and from Cabinet Office. Sadly, this pipeline has been shut off, as the Liberals formed a majority government after the last election, and continually vote to block access to any further information.

Shockingly, the documents we were able to obtain confirm the government is not being honest about the state of the province's finances. What the government is saying publicly about eliminating the deficit, and what they discuss internally, are two very different things.

These internal government documents – kept secret by the Liberals until revealed through exhaustive research by the Ontario PC Party – confirm that the Premier and the Finance Minister have no plan to stop their Greece-style accumulation of debt, despite the risk it poses to core frontline services like health care and education. But you don't need the documents to prove that – just look at the higher deficit and deeper debt of the past 12 months.

In one briefing document prepared as 'Confidential Advice to Cabinet', senior Finance officials repeatedly warn that the economy has not regained full strength since the recession, with higher unemployment and growth still dragging. This secret document stresses that the facts and figures presented in the 2014 budget are "a plan" and are really aspirational and notional figures with no substance behind them and confirms the government has no real plan to balance the budget.

In fact, the Ministry of Finance admits the benchmark of progress – an estimated $24.7-billion deficit – is a complete fiction, "was never a real expectation" and "was a deliberate policy" to project "a worst case outcome." In other words, it was deliberately misleading. They also admit "the path to balance was then drawn from there, assuming a straight-line trajectory of declining deficits", and "it was assumed that spending would be constrained to whatever it takes to hit these targets." Essentially, someone laid a ruler across a graph, drew a straight line, and that's the extent of the government's plan to balance the budget. They also divulged, "Over the medium-term, we have notional targets by sector that add up to the deficit numbers, but not yet full plans to deliver on them. For the extended outlook, neither sector targets nor plans yet exist". The once-secret document concludes "in order to hit the deficit targets, spending growth going forward has to decrease dramatically". But as we've seen, that restraint never materialized.



Even after the first Liberal-NDP budget of 2012 received credit rating downgrades from Standard & Poor and Moody's Investor Service, the Liberals continued to rack up debt. The documents warn that Ontario is the biggest single borrower among all states and provinces globally, and even if the government backed off its 2017-18 target for balancing the budget, it wouldn't do any good – even adding "6 more years" to the timeline.

The Liberal government has no plan to shift course from their race to the bottom. Jamison Steeve, Executive Director of the Institute for Prosperity and Competitiveness and the Martin Prosperity Institute at the University of Toronto, wrote in the Toronto Star, "Basically, Ontario's economy is not producing as much wealth as planned, hoped or expected." The report went on to say: "Ontario's prosperity gap with its North American peers is going in the wrong direction. In 2013, Ontario slipped to 15th out of 16 peer jurisdictions on GDP per capita. Furthermore, the prosperity gap increased by $180 from last year and now stands at $11,180. What does this mean? It means less money in the pockets of regular Ontarians. And it means less money in the public coffers to purchase the public goods that can improve the lives of all Ontarians."

Rating agencies signaled their concern last year by downgrading Ontario. In July, reflecting the growing debt burden and subdued growth outlook, Moody's Investors Service changed the outlook on Ontario's debt rating from stable to negative, affecting approximately $250 billion in debt securities. After failing to heed the rating agencies' spring warnings, the province was again downgraded by Fitch Ratings in December 2014 from AA to AA-, saying "difficult actions" will be necessary for the province to achieve its target of eliminating the annual deficit. In February, Moody's again warned Ontario about its debt burden, reporting that the province will have a more difficult time than Quebec achieving a balanced budget and paying down debt. They forecast that by the end of the year Ontario's government debt would equal around 244 times its total revenue.

It's time the Premier comes clean to the Legislature and the people of Ontario. She has been saying there is a plan in place, while her own senior Finance officials plead with her that it's not the case.

THE STATE OF ONTARIO

The majority of these pages will discuss Ontario's debt and deficit, and be filled with many numbers. So to ease you into it, let's start with a few anecdotal stories mixed in with some cold hard facts.

In January, 2014 and again in 2015, my Legislative colleagues and I toured Ontario in a series of pre-budget consultations and finance roundtables. All three parties met with business groups, social advocacy groups, and individuals. After visiting over one dozen cities, from Fort Erie to Fort Francis, a definite theme arose. Skyrocketing energy rates. New taxes. Crushing red tape.

We certainly knew that skyrocketing energy was a very important issue, and I'm going to spend the next 14 pages on that topic.

Given that the Liberals have planned to institute a carbon tax and a pension tax, we also suspected that these new taxes would dominate the conversation – and they did!

We've also been hearing from a lot of businesses that red tape is killing them, but the biggest surprise was hearing that from the social organizations as well.

It quickly became apparent that all is not well in Ontario. Let's start with energy.

ENERGY

In 2011, after serving my first three months as PC Energy Critic, it was apparent that while energy rates had doubled, they were about to skyrocket. The Auditor General had just presented his scathing report on the Green Energy Act and the Liberals showed no sign of changing course. I put pen to paper and in January 2012 the following column was published in Ontario newspapers.

Ontario Being Led Down Green Garden Path

> Sitting in the Mayor's chair in North Bay for seven years afforded me plenty of opportunity to interact with provincial politicians. I raised an eyebrow a couple years ago when I first heard an MPP use the expression "dirty coal" at a non-energy announcement. Then I noticed each Liberal MPP worked the phrase into their speeches, regardless of the topic. As a life-long marketing executive, I cracked a smile, knowing that this spin was laying the groundwork for the real hit. That came in 2009, in the form of a document entitled The Green Energy Act (GEA). The stated purpose was to 'green' Ontario's energy sector through conservation and renewable energy generation. To ensure that no one got in its way, the Government removed all municipal planning powers over the development of renewable energy generation.
>
> In many ways the GEA put the desires of the renewable power industry ahead of the needs of Ontario businesses and electricity consumers.
>
> For instance, when you neutralize the municipality (the public's only forum to fight a rezoning), toss around phrases like "dirty coal" (which stifles naysayers), and put a 'green' label on it (which minimizes opposition), you've got a perfect storm for procedural abuses, failed fiscal oversight, and gross misuse of taxpayer dollars.
>
> Now, as a newly-elected MPP and PC Energy Critic, I've spent the past three months meeting with industry stakeholders from all sides, assessing the GEA.

It will be no surprise to anyone who pays a hydro bill, that I believe the GEA to be a complete disaster. What may surprise you are some of the people who agree with that assessment. Here's a quick recap of what has happened with power, under Premier Dalton McGuinty.

The Feed-in-Tariff (FIT) Program pays out massive subsidies for wind and solar contracts to produce power we don't need. This continues to drive up the cost of electricity – it rose 26 per cent between 2008 and 2010. It is projected to rise another 46 per cent by 2014.

Even McGuinty knew what would happen next. Years earlier, while serving as Energy Critic he stated, "I am not going out on much of a limb when I say there is a direct correlation between hydro rates and our rate of unemployment in Ontario. As the rates go up, so will the rate of unemployment."

As a result of skyrocketing energy prices, manufacturing plants, forestry mills, and mineral processors close and move to where they find cheaper power. In Timmins, a city of 43,000, Xstrata Copper axed 672 employees and moved just across the border to set up shop in Quebec, where hydro is cheaper. It affected another 4,000 employees province-wide.

In total, Ontario has lost 300,000 manufacturing jobs in recent years. This has resulted in even lower demand for hydro, and we now generate far more power than needed. Unlike a commodity, you can't store electricity. So we pay the U.S. and Quebec to take this surplus power off our hands. We've paid them $1.8 billion over the past six years; $420 million in the first 10 months of 2011 alone. Their industries use this cheap power to compete even harder with our manufacturers, and so the downward spiral continues.

If the province stays on this current path, your hydro bills are going to increase dramatically.

Auditor General Jim McCarter delivered a scathing indictment of Dalton McGuinty's energy policy. He found that wind generators operate at 28 per cent capacity and that wind output was out of phase with electricity demand during certain times of the day. Solar generators operate at just 13 per cent capacity. And the FIT Program, with its overly-generous payments, will cost taxpayers $4.4 billion more than the previous Standard Offer Program. In 2010 wind and solar accounted for 1,700 MW and the target for them is to produce 10,700 MW by 2018. The very problem that has sent our hydro bills skyrocketing and gutted our manufacturing sector is about to get six times bigger. The AG also told us that billions of dollars were committed to renewable energy without fully evaluating the impact through a comprehensive business-case analysis. No independent, objective, expert investigation had been done to examine the potential effects of renewable-energy policies on prices or job creation.

Even Dr. Patrick Moore, co-founder of Greenpeace, weighed in recently with his comment that the wind power industry is "a destroyer of wealth and negative to the economy." He went on to say that wind farms are "ridiculously expensive and don't work half the time."

George Smitherman, former Liberal Energy Minister and architect of the Green Energy Act, spoke out recently. He feels that maybe the price paid for FIT contracts needs to be adjusted, and that perhaps municipalities should not have been cut out of the picture. At the launch of the GEA, he said it could lead to a modest increase in electricity bills of about 1 per cent annually. The cost you paid for electricity went up an average of 9.8 per cent last year. Without an immediate cancellation of the FIT program, look for that to continue.

Next, look for the words 'Global Adjustment' on your hydro bill. Simply put, Global Adjustment covers the spread between market price and guaranteed price paid to generators, plus the cost of paying standby gas plants not to produce electricity, as well as paying for conservation programs. This will be the hottest energy topic for the next several years. One North Bay manufacturer showed me that the

Global Adjustment, nonexistent on their 2009 hydro bills, is now $1,700/month, while their electricity charge is $1,400/month. Another hometown company's annual Global Adjustment is seven figures – for a line-item they never factored into their budgets. The Global Adjustment is expected to increase tenfold, from $700 million in 2006 to $8.1 billion in 2014. This will certainly cause more Ontario manufacturers to close up shop and move to cheaper locales.

Also, watch for the Smart Meter charges to hit home. Environment Commissioner Gord Miller weighed in recently, reminding us that reducing peak demand was the prime driver for introducing smart meters in the first place, yet there is no data to show if it's helping consumers conserve. The computer system that runs the Smart Meters cost $250 million, and the bill is now due. Your local utility will be adding 75 cents a month to repay that purchase. And where a traditional meter costs 65 cents to read, these electronic meters cost $1.50 plus another 90 cents for the towers and controllers. In addition, your local utility will be adding a $1.50 monthly fee to pay for their share of the $1 billion spent on the actual Smart Meter units. Total it all up and you'll see a further $4.00 a month added to your bill this year.

Let's not forget the cancellation of the Oakville power plant and cancelling, demolishing, and relocating the Mississauga power plant. These cancellations were nothing more than political 'seat savers' and may cost taxpayers $1 billion. That bill will come due this year, followed by the bill for the new plants, once the government figures out where to locate them. This comes at a time when industry experts are questioning the reliability of the GTA power grid.

The path this government is on will continue to be destructive to Ontario. By contrast, the PC Party will get rid of the fantasy energy world of the GEA. We will end the unnecessary and unnecessarily rich subsidies to the few in the renewables industry and go back to a power system built to supply the people of the province with reasonably priced electricity.

Remember, that column was written at the end of 2011 – it's remarkable how accurate those predictions were – especially the billion dollar prediction of the gas plant cancellations and Global Adjustment hitting $8 billion by 2014 (it reached $7.7 billion)! Any government paying attention would have known the financial mess it created.

What we saw was a government with a social engineering plan in mind – the Green Energy Act. When this disaster started, Ontario produced 25 per cent of its energy from green energy – water power – the cleanest, greenest, most reliable and affordable source of renewable energy. Now, several years and $50 billion later, Ontario still produces 25 per cent from green energy; 22 per cent from water and 3 per cent from wind (Ontario Energy Board, January 2015). There is absolutely nothing green about their version of green energy.

Since writing that column, a few more facts have surfaced, including more details on the Global Adjustment charge. The Auditor General pointed out wind generators operate at 28 per cent capacity and wind makes energy mostly at night when we don't need the extra power. So we have been paying Quebec and the U.S. to take that surplus power. In her recent report, the Auditor General estimates that between 2006 and 2013 the revenue from selling surplus power was $2.6 billion lower than what it cost Ontario ratepayers to produce it. Whenever wind does blow during the day, and power is produced, the government is contracted to take that power. But not knowing whether wind would generate power that day, they would have already contracted for all the power they needed. So they spill water over Niagara Falls onto idle generators, costing us about $300 million annually not to produce power.

And when that reduction is maxed out, they turn to nuclear plants, and redirect the steam away from the generators and vent it outside. That little exercise, done on five different days last year, cost the ratepayers $80 million. Add together the $500 million lost to Quebec and the U.S., the $300 million in spilled water, and the $80 million in vented steam, and that's almost $1 billion in extra payments due to wind power, or 'the law of unintended consequences'. In fact, the Auditor General estimates that between 2006 and 2015 Ontario ratepayers will have paid $50 billion to cover the cost of paying generators a premium for their output compared to what it would sell for on the province's wholesale electricity market.

Wind proponents will quickly tell you that because only 3 per cent of Ontario's power came from wind, it was not their fault your hydro bills skyrocketed. They are not accounting for the above-explained money wasted as a consequence of wind-generated power contracts; and that's the billion dollars added to the Global Adjustment. When all this started, electricity sold for 4.3 cents per kilowatt hour in 2003. Today, at peak times of day, energy sells for 14.4 cents per kilowatt hour – more than triple the 2003 hydro rates.

The Auditor's General are not alone in their concerns. Here are some worldwide headlines: Italy Cuts Solar Subsidy; Dutch Pull Plug on Wind Subsidies; UK Solar Subsidies Slashed; Germany Slashes FIT; and Spain Halts Renewable Subsidies to Curb $31 Billion of Debts.

> *The Auditor General stated the FIT program loses two to four manufacturing jobs for every so-called green job created.*

While other jurisdictions are realizing what a disaster this has been, Ontario is still doubling down. When the column was written, wind and solar accounted for 1,700 megawatts of power, and the target was to produce 10,700 megawatts by 2018. The very problem that has sent your hydro bills skyrocketing and gutted our manufacturing sector was set to get six times bigger! Because of so much community pushback on these installations, whether for health concerns, property values, environmental reasons, and a whole host of community activism, there has been a partial retreat and the target has been re-set down to about 6,500 megawatts. However, there's no comfort in knowing the problem is only going to be four times greater!

The retreat by the Energy Minister to reduce FIT subsidies and give token input to municipalities is an admission their energy plan is a failed social experiment. But reducing the subsidies will NOT solve the problem. The Liberals will still be spilling water, venting steam, and draining jobs into Quebec and the U.S.

While the government claimed the Green Energy Act would create 50,000 jobs, the Auditor General stated the FIT program loses two to four manufacturing jobs for every so-called green job created. In Timmins, Xstrata Copper, Ontario's single-largest user of power, moved their smelter 115 kilometers across the border into Quebec, lured by low hydro rates, and terminated their 672 Ontario employees. This should have been a warning to the government. Instead, we now have hundreds more examples of companies leaving Ontario for cheaper power, and there are more added every single day.

There are also companies that simply will not locate in Ontario because of our high hydro rates. The Montreal Gazette revealed that Innovation Metals, a Toronto-based firm, announced plans to set up the world's first independent centralized rare-earth ore separation plant in Becancour, Quebec. The company chose the location over several potential sites in Ontario citing Quebec's low industrial power rate as a major factor. It's estimated the rare-earth metals refinery will require an investment of more than $200 million and the creation of about 300 new jobs. Furthermore, according to a recent Ring of Fire report released by the Ontario Chamber of Commerce, current electricity rates make it so there is no business case to locate a ferrochrome smelter or stainless steel plant in the province.

Clearly, the province's competitiveness suffers from its high electricity prices for industrial users. But it's also affecting the commercial sector, according to a Canadian Federation of Independent Business survey. The report stated "97 per cent of small businesses are concerned about the current state of Ontario's economy, with 67 per cent very concerned." It also stated "93 per cent wanted the government to reduce energy costs".

In December, 2014 we learned that the government's green energy project has gone even more off track. The Auditor General released her annual report outlining how the overall costs related to implementing smart metering in Ontario had reached $1.9 billion – twice the original estimate. The report also noted that the government's stated objective of reducing power demand at peak times is not being met. The Minister of Energy, Bob Chiarelli, shocked reporters after Auditor General Bonnie Lysyk presented her annual report by stating, "Why are my numbers more credible than hers? First, the electricity system is very complex, is very difficult to understand", suggesting the Auditor General, who had a decade of experience at Manitoba Hydro, an MBA, and CPA designation, just didn't get it. Most recently, the program was awarded the provincial 'Teddy' award from the Canadian Taxpayers Federation for government waste.

Professor Ian Lee of Ottawa's Sprott School of Business summarized Ontario's energy situation in a Toronto SUN article. "Over the last eight years, the government of Ontario has squandered an energy-competitive advantage that keeps the province competitive with northeastern U.S. states, such as New York, Pennsylvania, Michigan, and Ohio," he said. Failed Liberal policies mean we've lost that competitive edge. "The government squandered it to drive up energy prices by subsidizing people at 10 times above the market price to put in solar panels to produce a surplus of electricity – that we didn't need in the first place – which we then sold at a loss to the Americans to exacerbate the competitive advantage we have handed them by squandering our cost advantage on energy," he said.

We'll give the last word on this to Carol Goar of the Toronto Star, as she sums up the Liberal's Green Energy Act. "The rollout was costly and ill-conceived. It drove up electricity prices, undermined public support for wind and solar power, riled rural Ontarians, and left a trail of aggrieved investors and producers".

Gas Plant Scandal

Any chapter on energy wouldn't be complete without mentioning the Liberal Gas Plant Scandal. It tells you all you really need to know about what is in the heart of, and what drives the Liberal Party of Ontario and the McGuinty-Wynne Government. Ontarians wanted to know the answers to two key questions – how much did the cancelling of the two gas plants cost, and who ordered the cover-up. The Auditor General answered the first question, but we still don't have the answer to the second. It shouldn't have to take an OPP criminal investigation and the threat of jail doors slamming to get that answer. Unfortunately, while Premier Kathleen Wynne continues to talk about being open and transparent, she is doing the exact opposite.

Using her new majority government, she has shut down the Gas Plant Scandal committee, not allowing the final witnesses to appear. Meanwhile, two OPP search warrant applications have been released confirming that deliberate efforts were made to keep government information secret. The documents name Premier McGuinty's former Chief of Staff and several other key staffers in the former Premier's office as complicit in deleting vital Gas Plant Scandal Documents.

You may find a little hyperbole and vitriol in these next couple of pages. After all, as the PC lead for most of the Gas Plant Scandal, I had a front-row seat. Working through summer and winter Legislative breaks, with daily meetings and twice-weekly televised Hearings, we faced an entrenched Liberal opposition. Premier Dalton McGuinty mocking me didn't help. After I first announced in the Legislature that this would be another "billion dollar scandal", the then-Premier responded in the London Free Press, "I am waiting for the day when somebody says, 'Actually it's $400 trillion'. What was the latest number? $1.3 billion? Do I hear 1.7? When are we going to get to 2.8? It's kind of an interesting game. In total we are talking a $230-million cost."

By $230 million, he was referencing the $190 million for Mississauga and $40 million for Oakville the Liberals claimed was the total cost to Ontarians. The two Auditors General released their findings which proved it actually cost $275 million for Mississauga and

$815 million for Oakville – totaling $1.1 billion, the estimate we announced in 2012, which the now-disgraced former Premier mocked!

A little history

It was in October, 2010 when the Liberals cancelled a contracted gas power plant in Oakville. Then in September, 2011, with Kathleen Wynne as co-chair of the Liberal election campaign, a decision was made just days before the election to cancel a similar but smaller plant already under construction in Mississauga. There was public opposition to both plants in the locations where they were supposed to be built from day one. The Liberals didn't listen and forged ahead. It was only when they realized they could lose five seats in the 2011 election that they changed course. Kathleen Wynne herself has admitted the cancellations were "a political decision." As we now know, Ontarians are paying dearly for this latest Liberal scandal, to the tune of $1.1 billion.

While the Oakville plant never broke ground, there was an approved contract. Documents released to the Standing Committee on Justice show the political considerations that led to the decision to cancel the plant in 2010. They also detail meetings between senior staff in the Premier's office in which the proponent believed they were promised to be "made whole" – or compensated for the full value of their 20-year contract. When then Energy Minister Brad Duguid met with the proponent two days before the announced cancellation, he had no idea such a deal had been offered. He was out of the loop. Documents show the proponents then "blew a gasket" and told Duguid to "go talk to your bosses".

This set in motion months of negotiations. At one point, a deal was in place to move the plant to Cambridge, but it was never consummated. The most telling document is the one showing that in April, 2011, the proponent had rejected a second counter-offer worth $712 million. This was key because when the Premier tried to tell Ontarians the Oakville cancellation only cost $40 million in September, 2012, it wasn't logical or believable. No one is going to turn down a $712 million offer to settle for $40 million.

Later we would learn that Cabinet, with Kathleen Wynne as Chair and with her signature on the document, would sign off on "Project Vapour" – essentially a process that wrote a blank cheque in order to reach a deal. In essence, the deal was to move from the court system into a private arbitration venue where the proceedings and the results would be kept secret. In order to secure an agreement, the Liberals waived valid defences and gave up the benefit of judicial limits on damages. The Liberals hid the majority of the settlement costs on the hydro bill, while only talking publicly about the much smaller taxpayer portion of the costs.

Cabinet, with Kathleen Wynne as Chair and with her signature on the document, would sign off on "Project Vapour" – essentially a process that wrote a blank cheque in order to reach a deal.

While the Oakville plant never broke ground, the Mississauga plant was already partly built when that cancellation was announced. But construction continued on the site for nearly two months as the proponent had a contract, and intended to fulfill it. Construction only stopped after the Government made concessions in 10 "side deals", as the Auditor General phrased it. These questionable side deals drove up the cost of the Mississauga cancellation. The Government first insisted the cost was $180 million, then $190 million. The Auditor put the final cost at $275 million, because those side deals added another $85 million onto hydro bills.

In both cases, the costs were driven up because of where the Liberals, and Liberals alone, decided to relocate the gas plants. The Mississauga plant is now to be built in Lambton, while the Oakville plant is to be constructed near Napanee. Because they're being moved so far away from where the power is needed – the southwest Greater Toronto Area – and in the case of Napanee, far from the source of the natural gas, the costs soared dramatically. The Auditor General testified before the Justice Committee that the Liberal decision to move the Oakville plant so far away from where the power is needed, was responsible for $513 million in added costs – nearly half of the total scandal cost!

Just getting the documents to piece together the real story of this scandal revealed the true nature of what drives the Ontario Liberals. In May, 2012, my former colleague MPP Rob Leone of Cambridge asked the Energy Minister a simple question before the Estimates Committee – what did it cost to cancel the Oakville and Mississauga power plants? The Minister refused to provide an answer. So a motion was passed compelling the government to turn over documents related to the cancellations within two weeks. The deadline came and went – no documents. This was our first clue the government had something to hide – and as time would show us, had lots to hide.

Only under the threat of being found in Contempt of the Legislature did the Energy Minister finally release the documents four months after the initial request. At that time, we were told we had all the gas plant documents. Then, two weeks later, shockingly we received another 20,000. Mr. McGuinty shut down the Legislature and resigned as premier three days later setting the stage for Ms. Wynne to take over. We would later hear sworn testimony that an Energy Ministry staffer with long-held Liberal ties, was sent to the Ontario Power Authority to instruct them to withhold certain documents. Then in February 2013, even more documents came forward. And later, even more. The total, according to Premier Wynne, is now over 300,000 – that's 18 months after being told the 36,000 were all the documents!

It was testimony to the Justice Committee that helped reveal the most unseemly side to this story. The former Chief of Staff to the Energy Minister admitted he regularly deleted emails. We now had proof that there was indeed a cover-up, as we alleged from the day they tried to pawn off the 36,000 documents as 'everything'. That led to an investigation by the Privacy Commissioner, who revealed there had been a widespread attempt by senior staff in the Premier's office to delete and destroy records. She concluded "laws had been broken."

I called the OPP to report a crime – the theft of data belonging to the people of Ontario. MPP Rob Leone and I wrote to the Commissioner of the Ontario Provincial Police to file a criminal complaint. In the year since, OPP investigators have visited Premier Wynne's office, executed a search warrant at a data storage warehouse, executed a further search warrant, and have recently been awarded a warrant to explore a senior government official's BlackBerry.

As a result of information obtained from the first warrant, the OPP allege the former Chief of Staff to the Premier instructed the boyfriend of his Deputy to wipe 24 computers within the Premier's office. To accomplish this, he's alleged to have provided the boyfriend with global access to override passwords.

As a result of information obtained from the second warrant, the OPP told us $10,000 of taxpayer funds was paid to this boyfriend to delete the Gas Plant Scandal files. The Liberal Party of Ontario repaid the $10,000 – an admission they did pay to destroy evidence.

Sadly, the government still has refused to turn over many more documents the now defunct Committee had requested. They've admitted there are thousands of back-up tapes where deleted emails relating to the gas plant scandal could be located, but still have not produced them. More than 1,200 of those back-up tapes belong to Kathleen Wynne. We're still waiting for those emails to be produced and now they likely never will be.

> *The cover-up is more sinister than the original cancellation of the gas plants.*

The most sobering lesson of the gas plant scandal may be this – if the Liberals had won just one more seat in the 2011 election, none of this would have ever come to light. The Liberals would have retained their majority. Any attempt at Committee to get documents would have been voted down by the Liberals; the Gas Plant Scandal hearings would never have happened. The Liberals have tried to stall, delay, and thwart us at every turn in our bid to get to the truth. They cannot be trusted. They have consistently put their own interests, and the interests of the Liberal Party, ahead of the people of Ontario. And now, using her majority government, Kathleen Wynne has shut down the Gas Plant Scandal Committee and we may never get to the truth.

While we still search for answers regarding the cover-up, we do know this self-serving act cost the people of Ontario – as taxpayers and as ratepayers – an astounding $1.1 billion. Part of that cost has already shown up on our skyrocketing hydro bills, and more will be added as the terms of settlement dictate.

The two Auditors General who were involved stated it best. In referencing the Mississauga Gas Plant cancellation, AG Jim McCarter stated, 'The people of Ontario will have essentially paid for two power plants, but have just got one." On the Oakville Power Plant cancellation, AG Bonnie Lysyck said, "The gas plant cancellations cost "significantly more than may have been necessary" because of a number of what she calls "questionable decisions" by the Premier's office.

NEW TAXES

Liberals love to tax and spend. They believe it is good for the economy to add a Health Tax or HST – remember it was supposed to add 600,000 jobs! They believe it's their privilege to spend your money on things like wind energy, ORNGE, cancelling gas plants, and bailing out the MaRS real estate deal. Sadly they continue to spend more than they take in, so they have borrowed annually and grown out debt. The increased taxes and debt load have burdened the economy to the point we have lost 300,000 manufacturing jobs in the past decade and have seen 8 years with unemployment higher than the national average.

There are a number of other factors at play. You've just read how we got to the highest energy prices in North America. We have the highest payroll taxes in Canada. Our corporate taxes, which were scheduled to fall from 11.5 per cent to 10 per cent in the 2012 budget, were left at that level, as part of the Liberal's deal with the NDP, to win their support. But with so much Liberal spending in place, it's still not enough revenue. Two years ago the deficit was $9.2-billion. Last year it grew to $10.5-billion. And this year, the deficit skyrocketed to $10.9-billion. Our debt-to-GDP is scheduled to hit 41.2%.

There are a few other new taxes you may not have heard about yet. At the beginning of 2013, the Workplace Safety and Insurance Board required independent contractors and operators to pay WSIB coverage, even though most already have cheaper and better private insurance. Mandatory coverage for the construction industry under Ontario's workers' compensation system is tantamount to a tax on small businesses, independent trades people, and contractors. This is cutting into the earnings of small businesses and contractors, and for some, it could be the straw that breaks their financial backs. The legislation forces independent operators, sole proprietors, partners in a partnership, and executive officers of corporations in the construction industry, to now pay WSIB premiums. This is a tax on hard-working Ontarians designed to cover up the Liberal government's mess; a $14-billion unfunded liability at the WSIB.

Last year I held a news conference in my constituency office where local woodworker Steve Ciglen, painter Brent Tremblay, and general contractor John Best, were on hand. They all said they have long held private insurance that offers more extensive coverage and have nothing to gain from handing over a portion of their earnings to the WSIB. "This is a form of legal extortion," said Tremblay, describing the bill as "ugly" and "oppressive." He said the legislation, which requires him to pay premiums of between 7% and 8% on his own income, couldn't have come at a worse economic time. And Tremblay said additional costs for businesses will translate into higher prices for customers.

Best said most independent operators like himself, who already have insurance, aren't likely to make a WSIB claim against their own businesses. And the three local tradesmen also agreed that most independent operators will likely hang onto their existing insurance despite Bill 119, making the legislation that much more of an expense. Ciglen said his policy offers a rebate minus his claims after 20 years. And Best said his rates are based on a long history with his carrier – something he doesn't want to lose, especially in light of efforts to repeal the legislation. The three local tradesmen argue the law will only help to fuel the underground economy with cash-strapped operators and customers wanting to keep prices low.

If you really want to shake investor confidence, you can do what the Liberal government did to raise taxes in their 2007 budget. They made a sudden change to the tax structure for diamond mines, very close to the start of production at the Victor Mine, Ontario's first and only diamond mine. The diamond royalty, which works like income tax, would range 5% to 13% depending on annual production values.

At the time of the budget announcement, De Beers Canada had already invested approximately one billion dollars in the construction of the Victor Project, which was scheduled to start production in 2008. The De Beers Board and shareholders approved the Victor Project budget based on current policies and tax regimes including the fixed 5% Mining Tax Act rate for developments in the far north.

When the Liberals formed the government in 2003, Ontario was ranked the #1 mining jurisdiction in the world. Today we have fallen to #23. Is it any wonder? The government brought in the Far North Act, which cuts off half of Northern Ontario from exploration. This has caused many mining companies to pull up stakes in Ontario and head elsewhere where a more mining-friendly regime exists. You may have heard of the Ring of Fire. It's a mineral-rich area of land, about 300 km due west of Attawapiskat, rich with chromite (used in making stainless steel). Thankfully, it was discovered before the Far North Act was brought in, or we may never have found that site.

> *The Government proposed to introduce a diamond royalty system after De Beers Canada had already invested approximately one billion dollars in the construction of the Victor Project.*

I have toured the camps in the Ring of Fire on four occasions. While I was excited in 2011, it's depressing to visit there now. On my recent trip there were fewer than a dozen people working; down from over 250 at its peak. The problem? This government has dithered on participating with the infrastructure development. One company had invested over $700 million on the project. They have since left – not just the Ring of Fire, but have closed all their offices in Ontario. Another company has spent over $200 million drilling and delineating their ore body. They are ready to go into production. Sadly, on my last trip, they were down to a skeleton staff. When I asked why they were no longer drilling, they replied, "Why should we continue to spend our shareholder's dollars when there's no way to get the ore out to the market?"

Not only are the threats of new taxes and slow government response cited as reasons for lack of development in the Ring of Fire, but the CFIB also indicates red tape, in the form of the de facto moratorium on exploration permits, as a logjam that must be cleared. With all of these factors taken together, it is not surprising that the Frasier Institute's Mining Survey ranked Ontario 23rd internationally in terms of its attractiveness for mining – a drop of nine spots from a year ago.

This March, the Ontario Chamber of Commerce released a scathing report on the Ring of Fire. They call on the government of Ontario to "act now" to develop the region. They gave the province a failing grade for their lack of infrastructure and permitting delays, allowing activity and investment to grind to a halt. The Chamber warns, "Ontario needs to move quickly on development of the stalled Ring of Fire…or risk losing huge economic benefits".

Eight years have passed since this discovery of the century, and the government has done nothing (except hint that they may implement a Chromite Tax once the mines get into production). In my home town of North Bay, we had 66 mining and machining companies, primarily engaged in the exploration field. They supplied a lot of products to the Ring of Fire. Now that exploration has halted, many companies have had massive layoffs, and one company moved to New Brunswick for their lower business taxes, lower payroll taxes, and much lower energy costs!

Pension Tax

The government's Ontario Retirement Pension Plan (ORPP) is a wide-reaching payroll tax that will negatively affect businesses across Ontario and drive jobs out of the province. Maclean's magazine's Jason Kirby summed up the ORPP stating that "…while the details are still fuzzy, the plan will impose new payroll taxes on those businesses that don't already offer a workplace pension plan the government deems satisfactory. In short: bigger government and higher taxes. No wonder the Wynne government has to pay companies to move to Ontario."

The CFIB has come out strongly against the proposed ORPP on behalf of their members, stating that 86 per cent of small business owners surveyed did not support the plan. What's more concerning is that 69 per cent of these owners would freeze or cut salaries and 53 per cent would reduce their number of employees if the plan were implemented. A new survey of businesses from the Ontario Chamber of Commerce also indicates that only 26 per cent of businesses believe they can shoulder the financial burden associated with the ORPP. In their survey, 44 per cent of businesses indicated they would reduce their current payroll or hire fewer employees in the future. The Chamber is calling on the Government of Ontario to reconsider its proposed approach and further assess its negative impact on the economy. Alan O'Dette, President and CEO of the OCC, stated that "The ORPP is a blanket solution to a problem that requires a targeted approach."

Carbon Tax

Another new tax that threatens the manufacturing and business sector is the Carbon Tax. Many groups have raised concerns with the carbon tax implementation, including the Canadian Manufacturers & Exporters who expressed: "It will also be critical that Ontario not act unilaterally. Failure to act in parallel on a North American basis would put Ontario manufacturers at a significant competitive disadvantage." Ontario cannot afford to drive investment elsewhere. If the province implements a carbon tax we will lose high paying jobs and manufacturing investment.

I found Gwyn Morgan's Globe and Mail column, Wynne's green scheme could deal massive blow to Ontario and Canada, to be the best summary of what will happen. He notes the similarities between what's being proposed in Ontario and the carbon trading system that was established in Europe 10 years ago:

"As in Ontario, the story begins with huge subsidies for wind and solar power that drove up electricity prices precipitously. Cap-and-trade handed wind and solar power companies a second windfall by creating a 'carbon trading market' that allowed them to sell 'carbon offsets' from their low-emission projects. On the other hand, many factories and industrial plants, already struggling with high power costs, found it more profitable to shut down and sell their carbon credit allocation in the carbon trading market. As a result, the bulk of Europe's emissions reductions have been achieved by the departure of energy-intensive industries to overseas locations. Many of the products consumed by Europeans are now produced in countries without emissions limits ..."

RED TAPE

I prefer to call this chapter, Death by a Thousand Paper Cuts! From filing taxes to applying for government permits, how much does red tape cost you? At least $10 billion a year and a lot of stress. A report entitled Impact of *Regulation on Canadian Individuals*, for the first time, quantifies the cost of the most common red tape headaches faced by ordinary Canadians. The $10 billion figure takes into account the following:

- Complying with personal income tax obligations ($6.7 billion, excluding actual taxes paid);
- Applying for and renewing passports ($645 million);
- Applying for and renewing driver's licenses and vehicle registrations ($1.7 billion);
- And time spent complying with these and other regulatory obligations (excluding personal income tax)

> *The Government heard first-hand from small business owners in Ontario about how red tape cost them $11 billion a year.*

Businesses and consumers are both affected by red tape. Government rules, permits, and paperwork are involved in everything from renovating a home, to applying for a student loan, to going fishing. CFIB has previously pegged the direct cost of regulation on all Canadian businesses at $31 billion per year. The data on cost to individuals begins to provide a fuller picture of the total cost of regulation for Canadians. And in a series of roundtables with CFIB members in 2012, the Government heard first-hand from small business owners in Ontario about how red tape costs them $11 billion a year, and takes them away from their business and creating jobs.

The report also includes a public opinion poll in which almost half of the respondents said that excessive regulation adds significant stress to their lives.

Ontario also received a dis-honourable mention in the CFIB's Paperweight Award. The Ontario Ministry of Labour won the dubious distinction for making it mandatory for directors, owners, and independent contractors in the construction industry to buy the Workplace Safety and Insurance Board (WSIB) coverage. See last chapter!

As mentioned in the opening pages, throughout the dozens of cities all three parties visited, red tape was a common theme. We've been hearing from a lot of businesses that red tape is killing them, but the biggest surprise was hearing the same issue from the community organizations. Whether it was a Social Planning Council or a Poverty Action Group, the common phrase was "We can't send our case workers to the house, because they're busy filling out government forms for six hours a day."

In 1996, the Progressive Conservative government developed a Red Tape Commission to reduce red tape for small businesses and individuals and to promote business planning within the broader public sector. In addition to annual reviews of all regulations administered by every Ministry of the government, the Commission also initiated specific policy reviews, such as a 'Highway Incident Management Study' which sought to develop better coordination of emergency services dealing with highway accidents. Originally established as a temporary body, the Commission was re-constituted in 2000 as a permanent body. In December 2003, the newly elected Liberal government discontinued the Commission. Death by a thousand paper cuts!

DEBT AND DEFICIT

It took 23 premiers and 136 years to accumulate a debt of $139 billion dollars. It took Dalton McGuinty, along with his successor Kathleen Wynne, only 11 years to more than double that debt.

Over the past year, we have learned even more about the dismal state of our province's finances. According to the Auditor General, the net debt as a percentage of GDP will top 40% this year – about the same as Ukraine. Since the recession the per-person debt burden grew by an astonishing $7,800 to $21,000. The province already spends more on debt interest than on postsecondary education, and interest payments are continuing to increase by about 7 per cent a year, making them the fastest-rising cost for the government over the next four years.

Simply put – we spend far more money than we take in.

Remembering that this is taxpayer's money being spent, there is a philosophical difference at play. Liberals (and the NDP) want to tax and spend – with them deciding which projects get the spending. Conservatives believe that money should stay with those who earned it – the people and the businesses – and they will spend it, spurring the economy.

As an entrepreneur and fiscal conservative, I believe less government, lower costs, and fewer regulations are what create economic activity.

In the past decade in Ontario, we have seen just the opposite occur. Over the past decade, our government got much bigger; just look at bureaucracies such as the LHINs and the OPA (now merged into the IESO), each costing about $300 million.

We have new taxes; think the Health Tax, Diamond Tax, aviation fuel tax, and the coming carbon tax and pension tax.

And the Canadian Federation of Independent Business held a Red Tape Awareness Week showcasing the burdensome red tape in Ontario.

Businesses like to locate in a well-managed jurisdiction. They like to locate in places that have a lower overhead and encourage companies to make money. Those jurisdictions know that greater profits bring more investment and hiring. Today we have exactly the opposite of what is needed to create jobs and wealth in Ontario. We have more government, higher taxes, and more regulations.

The Ontario Chamber of Commerce recently released two reports. First, their guide to Ontario's debt and deficit situation entitled *How Bad Is It*? The title alone should give you some indication that it's bad – now we just need to calibrate how bad! They also published the 2015 version of their *Emerging Stronger* series. Both reports indicate the worsening economic climate for businesses in Ontario. For example, their Ontario Business Confidence Index found that only 29% of the 1,500 businesses surveyed are confident in the Ontario Economy in a global context, down from 42% in 2013. When you look at the sector-specific breakdown of those statistics one realizes that only 54% of energy/utilities sector is confident in their economic outlook, compared to 87% last year, and the average sector-specific confidence is 58%, down from 74%.

We have a government that absolutely loves spending other people's money to promote their own causes. The Gas Plant Scandal is a prime example. The government spent $1.1 billion dollars to save Liberal seats in the 2011 election. The Green Energy Act is another. This social engineering experiment resulted in Ontario going from being one of the cheapest electricity jurisdictions to one of the most expensive in North America. All this after spending billions of borrowed dollars.

Liberals believe that taxing you and spending your money will somehow increase economic activity, despite the fact that no other jurisdiction has achieved this goal. The results of their 11-year tax-and-spend binge speak volumes. But in spite of a horrible economic record, they're going to continue this practice, as promised by the Premier and the Finance Minister in the 2014 Fall Economic Statement. Jamison Steeve, Executive Director of the Institute for Prosperity and Competitiveness at the University of Toronto, summarized it in the Toronto Star as "Basically, Ontario's economy is not producing as much wealth as planned, hoped or expected". So we have more taxes and more spending coming. That means continuing deficits and growing debt.

Jean-François Wen, University of Calgary Professor of Economics and author of the Fraser Institute's Report, *Ontario's Debt Balloon*, calculates that 66% of the increase in debt since the 2008/09 recession is directly attributable to day-to-day expenses exceeding revenues on an annual basis. Wen writes, "Governments typically borrow money as a means to finance long-term assets such as roads, schools or hospitals. But in Ontario's case, the province has gone deeper into debt to pay for day-to-day expenses". Livio Di Matteo, Economist at Lakehead University, wrote that it's a "travesty" that in only one generation Ontario has declined from having Canada's strongest and most productive economy to having its weakest. This decline will only continue as the Liberals tax and spend plan continues to drive down private investment, suppress productivity and economic growth, kill job creation, and cause "a deterioration of ... public finances."

THE DRUMMOND REPORT

The Liberals needed to buy time and get themselves through the 2011 election. That's when they called on economist Don Drummond to recommend savings and reforms to Ontario's public service, so it could better deliver programs for the long haul.

On February 15, 2012 his 543-page Report, which suggested ending Ontario's unaffordable $1.1 billion electricity rebate and marginally increasing class sizes, was presented to the Legislature. In all, 362 recommendations warned that Ontario needs immediate action to avoid going down the path of Greece – and the options get a whole lot worse the longer we wait.

The Toronto Star's headline read "Drummond recommends a radical overhaul to get Ontario back to balanced budgets." The column went on to say "The Liberals and New Democrats have already challenged Drummond's extra gloomy economic growth and deficit projections."

> *Don Drummond called for a "sharp degree of fiscal restraint; take daring fiscal action" to balance the budget.*

Don Drummond outlined some big-ticket reforms that he said would be "an important turning point in the province's history." He called for a "sharp degree of fiscal restraint." He said "The government must take daring fiscal action early" and we must act "swiftly and boldly." To balance the budget will require "tough decisions" and the treatment will be "difficult" and "most of the burden ... must fall on spending." He called for "a wrenching reduction from the path that spending is now on."

Here we are, more than three years later, and the Liberals are planning further studies whether to take any of the urgent actions recommended by their own economist.

Two months after the Drummond Report was released, and two days after the 2012 budget passed, one of the world's major credit rating agencies downgraded Ontario, citing the province's swollen debt burden and tough economic times ahead. Moody's Investor Service's decision to downgrade Ontario came one day after another influential rating agency, Standard & Poor, issued a stern warning and a dimmer outlook. Previously it had downgraded Ontario from AA to AA-, similar to the downgrade from DBRS. Warren Lovely of CIBC World Markets commented that the province's rating could be knocked down further if it fails to stabilize its debt burden if it sees an unexpected deterioration in debt affordability.

The Auditor General has reported on the many consequences of high debt which includes the "crowding out" of other spending, a greater vulnerability to a rise in interest rates, and possible credit rating downgrades. Bonnie Lysyk stated, "At some point, the creditors will come knocking if the government keeps borrowing to pay its bills," and only weeks later they did. Both Moody's and Fitch rating agencies downgraded Ontario last year. Moody's also released a separate report in February outlining how Ontario's debt burden is in fact worse than that of Quebec's, because we have no plan for dealing with it.

There are two parts to any formula to get us out of the massive deficit hole the Liberals have dug: increased revenues and reduced spending. In the spring of 2014, the Bank of Canada issued a lower forecast for growth. It was a warning to the Liberals that their revenue targets may be in jeopardy. Instead of taking that into account, the Liberals passed the budget In July with their revenue figures unchanged. Then, just four months later, the government admitted it had fallen $500 million short of its revenue forecast and had to take a $300 million dip into the province's reserve fund. It should be concerning that their forecasts are so wrong in such a short period of time.

So in reality, we'll have less revenue and increased spending – exactly the opposite of what we need. (If you were following Ontario politics in 1991, this has a familiar ring. Bob Rae and his New Democratic Party tried it. Do I have to tell you how that worked out?)

Any family having trouble paying their bills knows you don't run out and buy a swimming pool. You don't go on a spending spree. Basically, what the Liberals proposed to do was use their MasterCard to pay off their Visa, and their Visa to pay off their MasterCard.

In response to the 2013 Fall Economic Statement, the Wall Street Journal reported that Ontario's fiscal situation is worse than California's and the province will have trouble hitting its deficit target. At the same time, the Globe and Mail called the Liberal plan "equal parts lunacy, desperation, and a return to failed 1970s-style state planning."

They added, "There is a very clear sense in which the Ontario government is playing 'blame the victim' for the sorry state of the provincial economy."

ONTARIO'S SPENDING

I first wrote about Ontario's deficit after former Finance Minister Dwight Duncan stated "I do not want Ontario to become like California". He said that about the same time the Fraser Institute published a report comparing deficits of the two jurisdictions. To research this thoroughly, I promised my wife a lovely 4-day trip to San Francisco where we would use that city as our home-base to tour three bankrupt California cities. We're still married. The result was my widely-published February 2013 column talking about deficits and other similarities.

California Dreaming; Ontario's Nightmare

> The dismal financial situations facing Ontario and California are clearly compared in a recently-released study. Both jurisdictions have crushing deficits of about $16-billion. Sadly for us, California is about three times our size, making it a fiscal darling compared to us.
>
> After reading many similar articles, I headed to California to see firsthand what Ontario might look like in the near future.

My wife Patty and I have fond memories from our many previous trips through California. You can imagine our surprise, this time, at the sight of garbage piling up along the highway between San Francisco and Stockton, the city that joined San Bernardino and Vallejo in declaring bankruptcy. These three are the tip of the iceberg – many more cities are teetering on the edge.

Assigning blame for California's problems depends on which side of the political spectrum you fall. The right points the finger at high public-sector wages and generous pensions and benefits. The left blames the bursting of the real estate bubble. What cannot be disputed is the fact that the cities in bankruptcy overspent. When assessments fell, revenues fell – and they couldn't pay their bills.

According to Michael Lewis, in his gripping book *Boomerang*, Vallejo is the city to pity most. *"The lobby of City Hall is completely empty. It's just a collection of empty cubicles. Eighty per cent of the city's budget – and the lion's share of the claims that had thrown it into bankruptcy – were wrapped up in the pay and benefits."*

Now, the City Manager runs the entire city of 116,000 with a staff of one. *"When she goes out to the bathroom she has to lock the door."*

On our trip, we passed hundreds of wind turbines as we drove to the historic community of Sonora. This is in the heart of gold country, established in the original gold rush of 1849. Today, thanks to expensive energy, the mines are closed and logging operations are silent. Museums were closed because of staffing cuts. The streets were empty. But we did see a lot of casinos!

The comparison to Ontario is inevitable. Mine processors here have closed – Xstrata Copper in Timmins shed 672 employees and moved to Quebec for cheaper power. We were the #1 mining jurisdiction in the world; today we've fallen to #28. The forestry sector is devastated – there are 60 closed mills today. The Far North Act has banned logging and mining exploration from another 225,000 square kilometres of land.

> As in California, wind turbines are popping up in rural Ontario. But our turbine owners are offered the highest subsidies in the world. This has caused energy rates in Ontario to rise to amongst the highest in North America.
>
> The Liberals have cancelled the slots-at-racetrack program, which netted the province $1.2 billion annually, opting to sprinkle 29 casinos throughout Ontario.
>
> I ask this simple question: Is that the best we can do?
>
> We have 600,000 unemployed in Ontario today. There are 300,000 fewer manufacturing jobs. These people need hope, not another short-term money grab by a government unable to control its tax-and-spend ways.
>
> California was once the ultimate realization of the American dream. Similarly, Ontario was once the engine of Confederation. Both have fallen on hard times, but as usual California is leading the way. If we heed the warning of Stockton, San Bernardino, Vallejo, and many other cities on the verge of bankruptcy, Ontario can lead again.
>
> And we can avoid turning the nightmare into reality.

Shortly after the California comparisons, we started to hear the word Greece pop up in discussions. In his book, *A Nation in the Red*, Murray Holland states, *"The Greek tragedy started ... when the government became the 'nanny' of the citizens. The handouts and freebies started, unions rose to power ... and the government spent more than it took in and borrowed the deficit. Because the government borrowed so much and put it into the economy by giving it to citizens, its debt mushroomed over the years, and interest expense ate away a substantial amount of the cash that was borrowed."* Sound familiar? I wanted to dig deeper into this, to present statistics on why Ontario was being compared to Greece. The result was my May 2013 column comparing the two jurisdictions.

My Big Fat Greek Ontario

I sat through the new Liberal Government's first budget, and all I can say is "Opa". We may well be on our way to our own Greek-style tragedy.

You don't need to be an economist named Drummond to know that Ontario is where Greece was in the 1980s. From 1984-94 Greece's net debt-to-GDP ratio went from 37 percent to 66 percent. Today Ontario is at 37 percent and if we maintain the spending status quo, we too will reach 66 percent by 2019.

The Drummond Report was a warning to Ontario: fix this now or it will destroy you. Instead, last year we saw spending actually up $3.6 billion, while revenue was up only $2.6 billion. We definitely don't have a revenue problem in Ontario; we have a spending problem.

Our debt is not a function of the global recession or tsunami, as I continue to hear in the Legislature. It's the refusal of the government to control spending, and their lack of political will to balance the budget. Low interest rates make carrying this large debt possible, but even the slightest increase in rates will cause trauma for the budget.

I recently attended a luncheon where the speaker, Niels Veldhuis, presented *Ontario's Debt: Surpassing California, Heading for Greece*? He told us that over the last 9 years, our GDP was up 3.3 percent while our program spending went up 6.6 percent. Had we just matched our spending to the GDP rate, last year's budget would have been $91 billion instead of $115 billion – and yes, that would have meant a surplus as opposed to a deficit.

The solutions to Ontario's problems aren't hard to figure out; they're just not easy to do. Ontario needs a government that has a plan to reduce spending and create jobs, and the courage to implement it. But it's hard to justify these tough decisions if people don't know how serious the problem is here in Ontario.

> The budget presented to Ontarians offers no reform, shows no sense of understanding the severity of our debt crisis, or the urgency required to fix the problem. It appears Ontario is headed to become the next Greek tragedy.

When the City of Detroit declared bankruptcy, the inevitable comparisons surfaced again, and I provided a summary of our similarities and my obvious conclusions. My 3rd finance-related column appeared in September 2013.

Ontario's Check Engine Light Is On

> The recent bankruptcy of Detroit is another warning sign to Ontario that without hitting the brakes, we too are headed for a fiscal cliff.
>
> Detroit, once the very symbol of industrial might, filed what will be the largest municipal bankruptcy in U.S. history. Their budget deficit is more than $380 million and their long-term debt is estimated to be $20 billion.
>
> The motor city's population declined from a peak of 1.8 million in the 1950s to 700,000. There are 78,000 abandoned structures. Police, fire, and ambulance services are unreliable – their fleets are in disrepair, and police response times average 58 minutes.
>
> In a letter approving the move, Governor Rick Snyder wrote "The city's creditors, as well as its many dedicated public servants, deserve to know what promises the city can and will keep. The only way to do those things is to *radically restructure* the city." He added the decision follows decades of decline for Detroit, "a period in which *reality was often ignored*".
>
> In many ways, Detroit is a warning light to the rest of the global economy, and especially to Ontario. Their debt is $27,000 for each resident. In Ontario, we each owe $20,000. Detroit is estimated to owe $9 billion for pensions and benefits.

Here, our unfunded pension liability is estimated at $100 billion; a problem that will only increase as Baby Boomers reach retirement.

But the Detroit bankruptcy is only the latest warning sign that Ontario is headed down the wrong road. Over the last year, several studies have been released making other comparisons.

Ontario is now where Greece was in the 1980s. Their net debt-to-GDP ratio went from 37 percent to 66 percent. Today Ontario's is at 37 percent, and if we maintain the spending status quo, we too will reach 66 percent by 2019.

Ontario and California also face similar dismal financial situations. Both jurisdictions have crushing deficits of comparable size. Sadly for us, California is about three times our size, making it a fiscal darling compared to us.

The Drummond Report proved to us the burden of eliminating our debt must fall on spending. It states, "To balance the budget, the province must target a spending level in 2017-18 that is 17 percent lower than the sum found in the Status Quo Scenario – a wrenching reduction from the path that spending is now on".

Instead of taking necessary action, the Liberals have taken us farther down the road with the same failed approach of the last decade.

The solutions to Ontario's problems aren't hard to figure out – they're just not easy to do. Ontario needs a government that has a plan to reduce spending and create jobs, and the courage of their convictions to get the job done. The Ontario PCs have put forward bold ideas in a series of 14 white papers to date, and stand ready to lead Ontario back from the brink into prosperity.

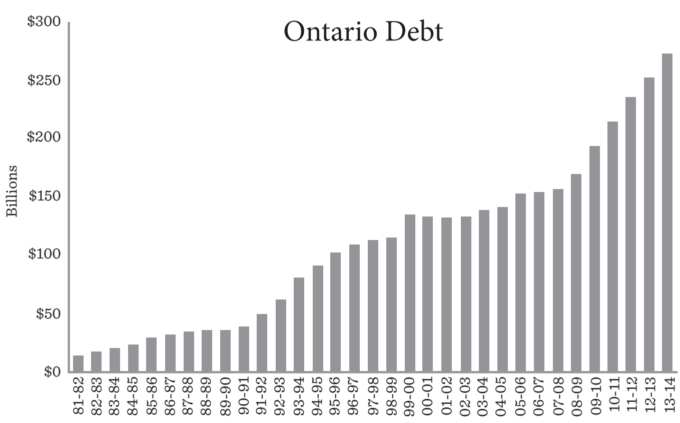
Without structural changes, our economy will be running on fumes – and we all know what comes next.

You've read philosophies on left vs. right; tax-and-spend vs. lower taxes, fewer regulations. They are philosophical differences. One can argue either side. But what can't be debated are facts, so when I became Finance Critic for the Ontario PC party, I began publishing Fedeli Focus on Finance. Six issues were produced in advance of last year's budget. Here is the issue dealing with debt and deficit.

Why Ontario's Spiraling Debt Matters

Ontario's fiscal problem is much deeper, and much harder to solve, than most people recognize.

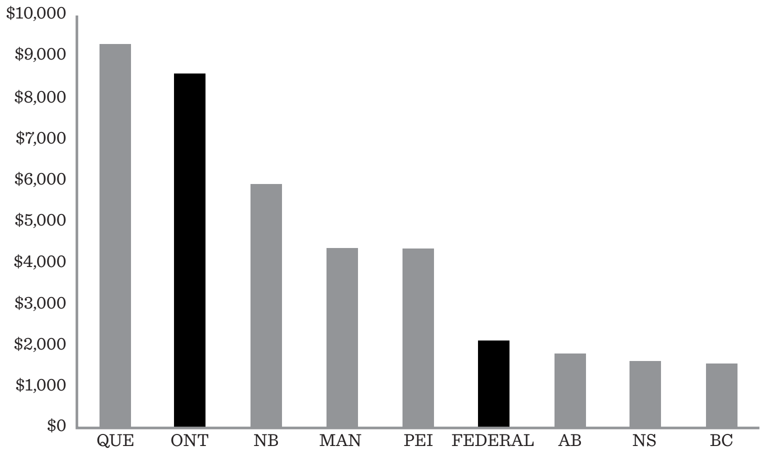
The debt is rising exponentially. In the last decade alone, it has doubled in size from $139 billion in 2003 to $273 billion in 2013. While it's understandable that a global financial crisis can push a government into debt, five years later we have to stop the pattern of overspending before it gets even further out of control. There is a common misconception that the current Ontario deficit is temporary because it was the result of "stimulus spending" that will soon disappear. However, the so-called "stimulus" of 2009 never went away. It simply got built into annual spending outlays, which are projected to continue indefinitely. As a result, Ontario's rapidly increasing debt will lead to rapidly increasing interest payments. We are likely to face rising interest rates in the coming years, which will make this problem worse. If we don't take action to address this problem, interest payments will soon crowd out core programs Ontarians care about.



Source: RBC Economics, Provincial Fiscal Tables, October 22, 2013

It's true that Ontario isn't the only province adding to its debt. The recession that spanned 2008 - 2009 caused a number of provinces to go into the red. But the amount of debt Ontario accumulated during this time is anything but typical. The government has no plan to address the debt problem. Without quick action, Ontario is heading towards a classic debt spiral.

Increase in Debt per Capita since 2003



Source: RBC Economics, Provincial Fiscal Tables, October 22, 2013

The government is adding an astonishing $20 billion to the debt this year alone. This includes the $12 billion deficit projected for 2013-14 plus capital expenses like infrastructure. This figure is little changed from the $24 billion added to the debt in 2009, when the Liberals tabled their massive "stimulus" spending budget. In other words, the government has barely slowed down the rate of piling on debt since the height of the financial crisis. "One-time" stimulus spending has become baked in as baseline spending.

An enormous amount of debt means we pay an enormous amount in debt interest. Currently, we pay about $10.4 billion every year just to cover our debt interest costs.

AT $10.4 BILLION, OUR YEARLY DEBT PAYMENTS ARE LARGER THAN:

What we spend on Community and Social Services ($10.2 billion)

What we spend on Training, Colleges and Universities ($7.7 billion)

What we spend on the Ministries of Energy ($340 million), Labour ($305 million), Environment ($495 million), Infrastructure ($350 million), Municipal Affairs and Housing ($789 million), Natural Resources ($715 million), Northern Development ($725 million), and so on.

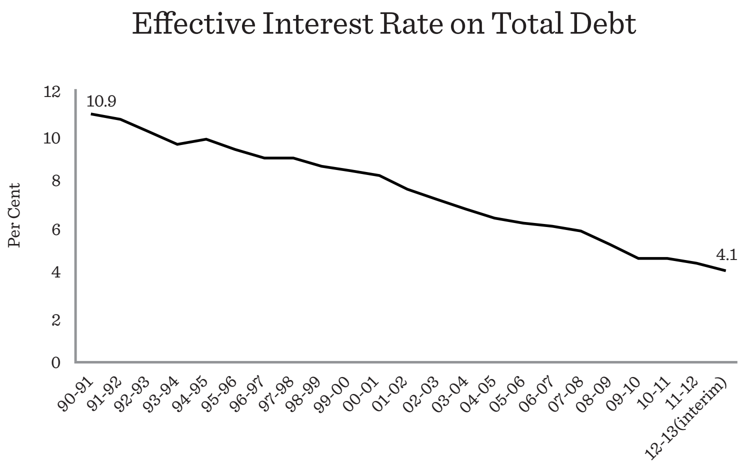
(Source: Budget 2013, page 223)

The most concerning issue about interest payments is the risk. What happens when interest rates go up? The 2013 budget gives us an indication of the consequences.

> *The 2013-14 impact of a 100-basis point change in borrowing rates is forecast to be approximately $408 million.*
>
> *-Budget 2013, page 212*

This means that if interest rates go up by one percentage point, then the yearly cost of our debt becomes $408 million more expensive. To put this amount of money in perspective, remember that the entire budget for the Ministry of Infrastructure is $350 million, and the entire budget for the Ministry of Energy is $340 million.

So far the province has been spared the real impact of rapid debt accumulation because interest rates happen to be low. In fact, interest rates are at their lowest point in 20 years. But this won't be the case forever.



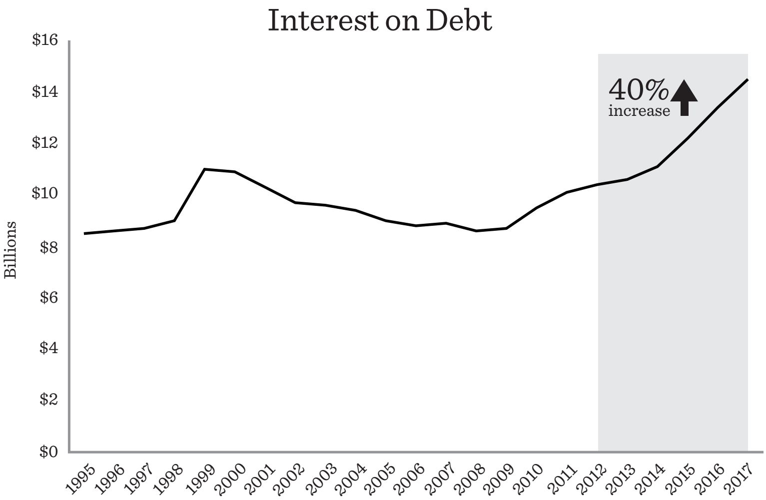
Source: Ontario Public Accounts (1991-2012) and Ontario Financing Authority

> *Debt is costly, since interest must be paid on the province's outstanding bonds and other obligations. Unusually low interest rates in recent years have allowed Ontario to borrow cheaply, but as interest rates rise to more normal levels, so will the cost of servicing the growing debt, and that will divert dollars away from public programs.*
>
> *-Drummond Report, page 2*

Even based on the government's most optimistic assumptions, debt interest costs are about to start spiking in the next few years, after remaining relatively flat for the last two decades because of low interest rates.

Debt interest will increase from $10.4 billion in 2012-13 to $14.5 billion in 2017-18, the year the government plans to balance the budget. This represents an increase of $4.1 billion, or 40 per cent in only 5 years.

As we get deeper into the debt spiral, the outlook gets even worse. That's because investors and credit rating agencies start to associate a greater risk to our debt, meaning we have to pay higher premiums in order to borrow money.



Source: Ontario Ministry of Finance

> *Given the extended period of consolidation and the ambitious expenditure targets, in Moody's view, there are significant risks surrounding the province's ability to achieve their medium-term fiscal targets and stabilize and then reverse the recent accumulation in debt.*
>
> *-Moody's Investors Service, 2012*

Why should we care what independent credit rating agencies say about our debt? As explained above, the government spends more money than it has, so it borrows the rest. Credit rating agencies like Moody's Investors Service, Standard & Poor's (S&P), Dominion Bond Rating Service (DBRS) and Fitch Ratings are all global firms that analyze the credit worthiness of a number of organizations, including government. The stronger the credit rating, the less risky it is for an investor to lend money to the government and usually the less expensive it is for the government to borrow. The weaker the rating, the more expensive it is to borrow.

RECENT ONTARIO CREDIT RATING DOWNGRADES

October 22, 2009: DBRS downgraded Ontario from AA to AA (low)
October 29, 2009: S&P downgraded Ontario from AA to AA-
April 26, 2012: Moody's downgraded Ontario to Aa2 (stable) from Aa1 (negative)

These various downgrades wiped away years of previous progress repairing Ontario's credit rating. Under the previous government, Ontario received four upgrades to its long-term debt rating and nine rating improvements in total.

(Source: Budget 2003, page 113)

Conclusion

The current government's rapidly growing debt payments pose one of the most significant risks to the province's ability to provide core public services.

Key Questions

What is the government's current projection for the amount of debt Ontario will accumulate between now and 2017-18, the target for balancing the budget?

Does the government's fiscal plan take into account the likelihood of further credit-rating downgrades?

Does the government plan to reduce spending in other areas to offset the increased debt interest costs? Or will the government simply issue more debt to cover these costs?

As I mentioned earlier, the results of the Liberals 10-year tax-and-spend binge are skyrocketing hydro rates, high taxes, and crushing red tape. But in spite of a horrible economic record, they're going to continue this practice, as promised by the Premier and the Finance Minister in the 2013 Fall Economic Statement. So we have more taxing and more spending coming. That means continuing deficits and a growing debt. Here is my Focus printed in response to the 2013 Fall Economic Statement.

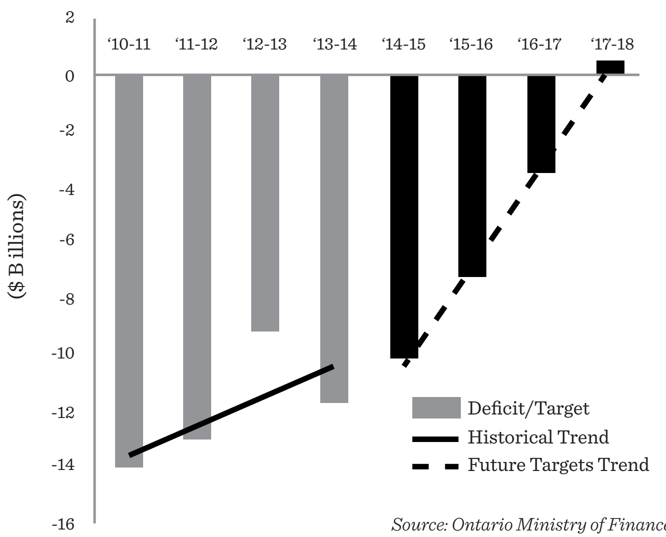
Ontario's Fall Economic Statement: No Plan to Balance

Last week's Fall Economic Statement, and the supporting comments by the Liberal government, went further than ever before in revealing the shift away from taking action to balance the budget that began when Kathleen Wynne replaced Dalton McGuinty as premier.

It is clearer than ever that the government has no plan to balance the budget, and for the first time, the government spoke openly about the possibility of not meeting even its own modest deficit reduction targets.

It's important to remember how we got here. When the government first faced deficits after the 2008 financial crisis, it announced a set of targets for returning to a

Ontario Deficit Trends



Source: Ontario Ministry of Finance data balanced budget, taking a full ten years before planning to balance in 2017-18. It did not, however, announce any plan for how those targets would actually be met. Critics observed that the announced plan delayed serious restraint to close the fiscal gap until the last few years of the plan, but the government asked for trust.

Until 2012, the McGuinty government refused to recognize that serious changes in policy would be required to close Ontario's unprecedented fiscal hole. But after the 2011 election, the McGuinty government began to acknowledge that it wasn't going to make it to a balanced budget – ever – on the track it was following. Most importantly, the Drummond Report concluded that at current course and speed, rather than balancing, "the deficit would more than double to $30.2 billion in 2017–18 and net public debt would reach $411.4 billion, equivalent to just under 51 per cent of the province's GDP." (Drummond Report, page 2)

The Drummond Report laid out a series of recommendations, all of which had to be implemented (or alternatives found) in order to meet even the 2017-18 target to balance. The government rejected some of Drummond's recommendations out of hand and turned away from the toughest measures.

It did begin to experiment, very tentatively, with a few restraint measures it had previously insisted were unnecessary, mainly by passing a legislative freeze on teacher pay, and circulating a draft bill to enforce a broader public sector wage freeze. But it still refused to lay out a specific plan for how to balance, or to acknowledge what specific restraint measures would be required.

After Kathleen Wynne replaced Dalton McGuinty as premier in 2013, the government's brief flirtation with restraint ended. The 2013 budget proposed a deficit that actually represented an increase over the previous year's deficit, from $9.8 billion to $11.7 billion. The government dropped the draft wage freeze bill, made unilateral concessions to undo the legislated teacher wage freeze, and stopped even talking about a wage freeze policy (see *Page 86* for more detail). The years with deficit targets that required real restraint were getting ever closer, yet the government was moving to less restraint, not more.

Budget 2013 did not present a plan to balance

Based on the 2013 budget, the Ontario PC Caucus calculated what spending restraint the government's targets implicitly required. Working from the expenditure totals presented in the budget, the analysis showed that even if the government achieved aggressive restraint in health, education, social services and justice, it would still need to cut everything else by 30 per cent in order to realize its balanced-budget target of 2017.

These deep, across-the-board cuts would target ministries such as transportation, environment, and municipal affairs and housing. We called this "the hole" in the government's fiscal plan, because there was never any explanation given for where these savings would be found. Each year as revenue projections are revised downward, the hole gets bigger and bigger if the government plans to balance the budget on schedule.

No Plan to Balance

	2012	2013	2014	2015	2016	2017
Total Revenue	**114.2**	**116.8**	**120.5**	**124.9**	**130.1**	**134.4**
Expense						
Health	47.8	48.9	49.8	50.8	N/A	N/A
Education	22.4	24.1	24.6	24.8	N/A	N/A
Post Secondary and Training	7.4	7.7	7.8	7.8	N/A	N/A
Children's and Social Services	13.8	14.3	15.0	15.2	N/A	N/A
Justice	4.0	4.1	4.1	4.1	N/A	N/A
Other	18.3	17.8	17.0	16.1	N/A	N/A
Total Programs	113.6	117.0	118.3	118.8	118.8	118.0
Interest on Debt	10.4	10.6	11.1	12.2	13.4	14.5
Total Expense	124.0	127.6	129.5	131.0	132.1	132.4
Reserve	-	1.0	1.2	1.2	1.5	1.5
Surplus/(Deficit)	**(9.8)**	**(11.7)**	**(10.1)**	**(7.2)**	**(3.5)**	**0.5**

Sources: 2013 Ontario Budget Pages 109 and 209

2013 Fall Economic Statement

Since real restraint would have to start within the next two years, the Fall Economic Statement was an opportunity to finally lay out the measures that would actually be required to achieve the more aggressive spending restraint needed for the last four years of the balanced budget targets. Instead, the government announced no new restraint measures at all, and hid the implications of this for the deficit outlook.

> *Ontario's revenues are more than $5-billion lower than projected since the 2010 Budget.*
>
> *-Ontario Finance Minister, November 7, 2013*

THE FOUR MAIN TAKEAWAYS FROM THE GOVERNMENT'S 2013 FALL ECONOMIC STATEMENT ARE:

1. **The economic assumptions upon which the province's finances are based have gotten significantly worse – particularly for 2013 and 2014.**
2. **The government plans to embark on a massive, second-round of debt-financed stimulus spending.**
3. **Despite the weaker economy, the government insists that revenue for this year will be virtually exactly the same as projected in the budget.**
4. **The government refused to provide the 3-year spending and revenue outlook traditionally included in the Fall Economic Statement, to hide the impact of a weaker economy and planned spending after March 2014.**

The following table outlines the changes in economic assumptions since the budget. Note that what matters to government revenue is nominal growth in the economy. This means you must take into account both the 0.2 percent drop in real GDP growth and the 0.4 percent drop in the Consumer Price Index.

Also note that economic growth for next year has been revised downward, which explains why this year's Fall Economic Statement differs from previous years in that it does not contain a Medium-Term Outlook. Primarily, this implies the government does not want to restate the projections for next year, where the government is expecting a further reduction in revenue and increase in spending.

TABLE 2.6 Changes in Ministry of Finance Key Economic Forecast Assumptions: *2013 Budget Compared* to *2013 Fall Economic Statement (FES)*

(Per Cent Increase)

	2013p		2014p		2015p	
	2013 Budget	2013 FES	2013 Budget	2013 FES	2013 Budget	2013 FES
Real Gross Domestic Product	1.5	1.3	2.3	2.1	2.4	2.5
Nominal Gross Domestic Product	3.0	2.5	4.1	3.8	4.2	4.3
Retail Sales	2.5	1.9	3.8	3.8	3.8	3.8
Housing Starts (000s)	61.0	59.0	60.0	58.0	65.0	65.0
Primary Household Income	2.8	2.9	3.9	3.6	4.2	4.4
Compensation of Employees	2.8	2.9	3.7	3.7	4.3	4.2
Net Operating Surplus - Corporations	3.3	(3.6)	5.0	4.6	4.0	4.2
Employment	1.2	1.5	1.4	1.4	1.5	1.6
Job Creation (000s)	83	104	98	97	107	114
Consumer Price Index	1.5	1.1	2.0	1.8	2.0	2.0
Key External Variables						
U.S. Real Gross Domestic Product	2.1	1.6	2.7	2.6	3.1	2.9
WTI Crude Oil ($ US per Barrel)	94	99	98	98	99	96
Canadian Dollar (Cents US)	98.0	97.4	99.5	96.5	100.0	97.0
3-month Treasury Bill Rate[1] (Per Cent)	1.0	1.0	1.2	1.1	1.9	1.9
10-year Government Bond Rate[1] (Per Cent)	2.0	2.3	2.6	3.0	3.2	3.3

p = Ontario Ministry of Finance planning projection.

[1] Government of Canada interest rates.

Sources: Statistics Canada, Canada Mortgage and Housing Corporation, Bank of Canada, U.S. Energy Information Administration, U.S. Bureau of Economic Analysis, Blue Chip Economic Indicators (October 2013) *and Ontario Ministry of Finance.*

And yet despite the slowdown in the economy, almost none of these changes affect the government's revenue projections. Consider the accuracy required to come within 0.0094 percent of your original revenue projection, when personal income taxes are expected to be $700-million lower, sales taxes $250-million lower and health premiums $70-million lower. The Federal government's Fall Economic Update showed the same slowing economy, and therefore showed $1.3 billion lower revenue than projected in its budget. If Ontario's revenue declined the same percentage as federal revenue, the deficit would have increased from $11.7 billion to $12.3 billion.

TABLE 3.1 2013-14 In-Year Fiscal Performance

($ Millions)

	Budget Plan	Current Outlook	In-Year Change
Revenue	**116,845**	**116,834**	**(11)**
Expense			
Programs	116,983	116, 970	(13)
Interest on Debt	10,605	10,605	-
Total Expense	**127,588**	**127,575**	**(13)**
Reserve	1,000	1,000	-
Surplus (Deficit)	**(11,743)**	**(11,741)**	**2**

Note: Numbers may not add due to rounding.

In fact, the in-year change for the 2013 deficit projection from the budget plan to the current outlook is a mere $2 million ($11.743 billion compared to $11.741 billion). Similarly, consider the accuracy required to come within 0.02% of this year's budget deficit projection, despite being off by billions of dollars when the auditor general reviews the actual results. The government has a demonstrated pattern of over-estimating its deficit projections in the budget, slightly revising those figures 6 months later and then "outperforming" their targets by 20-40 percent in the end.

Comparison of Original Budget Projections, Fall Economic Statements and Public Accounts Actuals

($ Millions)

	Original Projection	Fall Economic Statement	Actual	Difference btwn Original & FES	Difference btwn Original & Actual
2009	14,100	24,716	19,262	75.29%	36.6%
2010	19,690	18,656	14,011	-5.25%	-28.8%
2011	16,316	15,994	12,969	-1.97%	-20.5%
2012	15,153	14,371	9,220	-5.16%	-39.2%
2013	11,743	11,741	???	-0.02%	???

Source: Ontario Ministry of Finance, annual budgets, public accounts and fall economic statements, 2009 to 2013

No balanced budget plan

The most glaring omission from this year's Fall Economic Statement was the Medium-Term Outlook. That is a conspicuous change from normal practice, given that these projections are usually contained in this document.

2011 FALL ECONOMIC STATEMENT

TABLE 6 Medium-Term Fiscal Plan and Outlook

($ Billions)

	Actual	Projected Outlook		
	2010-11	**2011-12**	**2012-13**	**2013-14**
Revenue	**106.7**	**108.3**	**111.3**	**116.3**
Expense				
Programs	111.2	114.0	114.9	117
Interest on Debt	9.5	10.1	10.6	11.7
Total Expense	**120.7**	**124.1**	**125.5**	**128.7**
Reserve	-	0.2	1.0	1.0
Surplus (Deficit)	**(14.0)**	**(15.0)**	**(15.2)**	**(13.3)**
Net Debt	214.5	238.4	261.8	281.8
Accumulated Debt	144.6	160.6	175.7	189.1

Note: Numbers may not add due to rounding.

2012 FALL ECONOMIC STATEMENT

TABLE Medium-Term Fiscal Plan and Outlook

($ Billions)

	Actual	Projected Outlook		
	2011-12	2012-13	2013-14	2014-15
Revenue	109.8	113.0	116.6	121.6
Expense				
Programs	112.7	115.8	117.0	117.9
Interest on Debt	10.1	10.6	11.2	12.3
Total Expense	122.7	126.4	128.2	130.3
Reserve	-	1.0	1.2	1.5
Surplus (Deficit)	(13.0)	(14.4)	(12.8)	(10.1)

Note: Numbers may not add due to rounding.

2013 FALL ECONOMIC STATEMENT

(NO MEDIUM-TERM
FISCAL PLAN PRESENTED)

The Fall Economic Statement was also the first acknowledgement, albeit implicit, that the Liberal fiscal plan isn't working. In his address to the Legislature, Minister Sousa made it clear his government's priority is to continue to spend.

> *However, should global economic conditions falter, causing revenue growth to fall further, our priority is clear – this government will continue to protect investments in jobs and families* ***ahead of short-term targets****.*
>
> *-Ontario Fall Economic Statement 2013*

The government is saying they are going to continue to spend, when in fact the implication of their own budget targets – as shown earlier – is that they have to reduce spending growth across the board, and make 30% cuts in smaller ministries.

Then:

> *Ministries should be given seven-year spending targets regardless of the degree of overall spending restraint.*
>
> *-Drummond Report, page 95*

Now:

> *In the fall update, the government reiterated its commitment to return to budgetary surplus in fiscal 2017-18, but did not include a fleshed-out fiscal plan to get there.*
>
> *-TD Economics, November 7, 2013*

WHAT OTHERS ARE SAYING:

"As we have indicated in past budget commentaries, the task of taming expenditures will not get any easier in the years ahead." - RBC Economics, November 7, 2013

"In the wake of the financial crisis, the state of California has been something of a poster child for fiscal dysfunction, with years of budget deficits, service cuts and public-sector job losses. By some measures, though, the Canadian province of Ontario's fiscal situation is worse than California's, according to Moody's Investors Service." - The Wall Street Journal, November 6, 2013

Conclusion

The current government has said the economy will be worse. It has acknowledged it might not meet its targets due to continued stimulus spending. And then, suspiciously, it has refused to provide the standard information showing what the planning assumptions are for revenue and spending beyond the current year. Our conclusion is that the government is hiding the truth, because these figures would demonstrate the province is not on track to balance the budget by 2017-18.

Key Questions

What is the effect of the slowing economy on the government's current revenue, spending and debt projections for the next 3 years?

Why did the government deviate from the normal practice of including this information in the Fall Economic Statement?

I realize that this has been a complicated read so far. Sadly, it's about to get more complicated. You see, we have a hidden deficit in Ontario, and it's responsible for our growing debt. In a nutshell, about a decade ago, the government completed its shift to 'accrual' accounting. So now what shows up in the deficit is only the annual depreciation of all of our capital spending, not how much we actually spent constructing buildings and building infrastructure. This is fully explained in this issue of Focus.

Ontario's Hidden Deficit

Everyone who follows government policy is accustomed to explaining the difference between debt and deficit.

We repeat it endlessly: the debt is how much we've borrowed in total over many years, whereas the deficit is the net addition to the debt in just one year.

But if that's true, then how is it that our deficit is $11.7 billion, but our debt is going up $20 billion? If the deficit is the yearly addition to the debt, doesn't that mean our deficit is $20 billion?

Well, if the government were operating under the same accounting rules as Premier Rae and Premier Harris, then yes, the deficit would in fact be $20 billion, not $11.7 billion.

The government doesn't show this $20 billion figure, but it's easy to calculate from two numbers buried on page 221 of Budget 2013. You just subtract last year's net debt from this year's (the black circle minus the grey circle on the following page). This isn't a secret; it's hidden in plain sight. Bond traders know all about it.

2013 Ontario Budget (page 221)

TABLE 2.22 Medium-Term Fiscal Plan and Outlook

($ Billions)

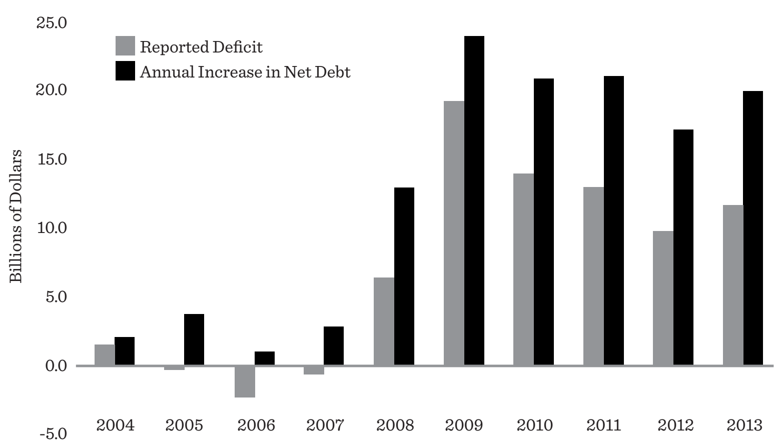
	Interim 2012-13	Plan 2013-14	Outlook 2014-15	2015-16
Revenue	**114.2**	**116.8**	**120.5**	**124.9**
Expense				
Programs	113.6	117.0	118.3	118.8
Interest on Debt[1]	10.4	10.6	11.1	12.2
Total Expense	**124.0**	**127.6**	**129.5**	**131.0**
Reserve	-	1.0	1.2	1.2
Surplus/(Deficit)	**(9.8)**	**(11.7)**	**(10.1)**	**(7.2)**
Net Debt	252.8	272.8	290.1	303.9
Accumulated Deficit	168.2	179.9	190.1	197.3

[1] Interest on debt expense is net of interest capitalized during construction of tangible capital assets of $0.2 billion in 2012-13, $0.3 billion in 2013-14, $0.4 billion in 2014-15 and $0.4 billion in 2015-16

Note. Numbers may not add due to rounding.

If we look at this over the last decade, we can see that Budget 2013 was not the only year the reported deficit and the annual increase in debt were not the same:

Deficit vs. Debt Increase



Source: Ontario Ministry of Finance

Note: in 2010, the government re-stated its historical net debt to reflect the consolidation of hospital, school board and college net debt with the province's. The re-statement only goes back to 2005-06 (when the original consolidation was done), so this analysis has been adjusted to eliminate the $8 billion increase in reported net debt that year, which was attributable to the consolidation.

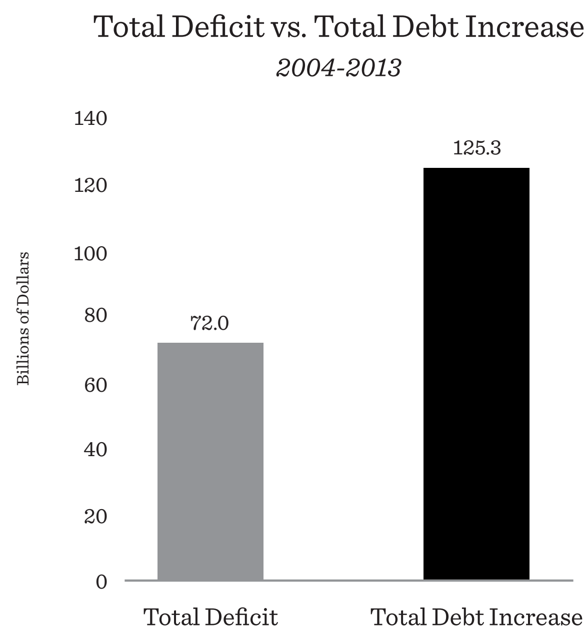
Now, how does that square with our story that the deficit is the amount that the debt goes up each year? How is it possible that we're borrowing an extra $20 billion in 2013, and that this is only 17 per cent less than the incremental borrowing at the peak of the global financial crisis in 2009 ($24 billion)? Is it really possible that the total deficits since 2004 are $72 billion, but the debt has gone up $125 billion over the same period? Why are the black bars so different from the grey bars – why is the deficit not the amount the debt increased each year, like we so often tell people?

> *We were never in real surplus – always borrowed*
>
> *-Secretary of Cabinet and Former Deputy Minister of Finance, Internal Cabinet Documents, November 11, 2011*

The reason is a quirk of accounting, and we should be paying as much attention to the black bars as the grey ones. WARNING: you now have to endure two paragraphs of accounting – but it really is an important point to understand.

Before 2002, the black bars and the grey bars were the same. The reason is that the government's accounting back then was more or less on a cash basis, meaning that with some small exceptions, the deficit really was the amount the debt went up each year.

Then about a decade ago, the government completed its shift to 'accrual' accounting. The biggest change in the new accounting system was in how capital investments like buildings and roads factored into the deficit calculation. Under the new system, instead of showing the cost of a building in the deficit when the money is actually spent (like we did until 2002), that cost is spread out over decades, and shows up in the deficit a little bit at a time over the life of the building. In other words, what shows up in the deficit is the annual depreciation of all of our buildings, not how much we happened to spend constructing and improving buildings in that particular year. It's like we automatically take out a mortgage on each year's capital spending, and the deficit only shows the mortgage payment.

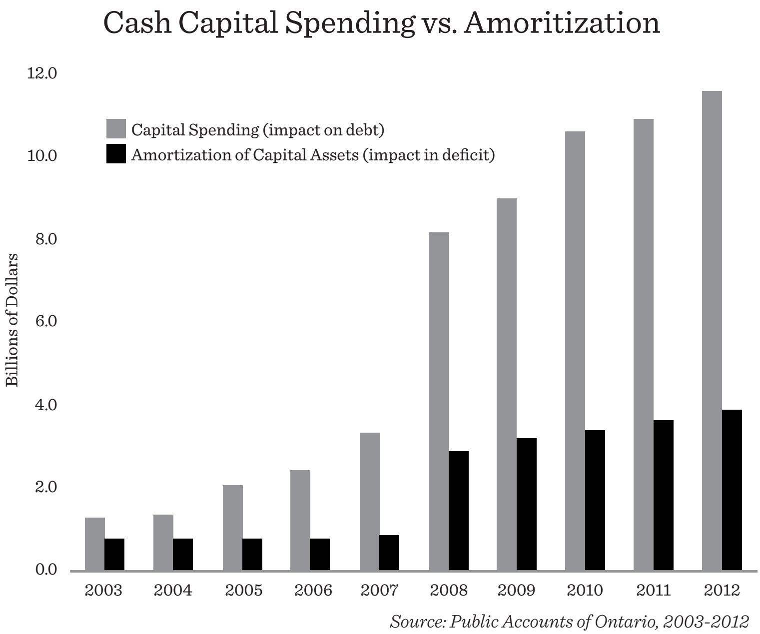


Source: Ontario Ministry of Finance

Capital Spending

So what do you think happened to capital spending once the full cost no longer showed up immediately in the annual deficit? The chart to the right provides the answer. The final numbers are never shown in the budget, but they can be found in the "consolidated statement of cash flow" in each year's Public Accounts. For obvious reasons, the government never shows the trend over time, so you have to look it up year by year in separate documents.

But we've done that for you.



Perhaps it should be no surprise that when the government no longer had to include the full impact of capital spending in the deficit, they increased capital spending. But what is shocking is the rate at which the government increased capital spending – nearly 800%!

By 2012, the government was able to spend $11.6 billion on capital, while only $3.9 billion of amortization – $7.7 billion less – showed up in the official deficit. Back in 2003, the difference was only $0.5 billion, less than 10% as much.

In 1994-95, when Premier Rae set what was then the record for the largest deficit ever ($10.8 billion), he had to include the full cost of capital spending in the deficit right away. He, or someone who cared about him, complained bitterly in the notes on page 6 of the 1994-95 Public Accounts about the unfairness of having to expense all capital costs right away, but nobody did anything about it for another eight years.

To be clear, there's nothing sinister about the new 'accrual' approach – it's consistent with how businesses account for capital investments. But if the government suddenly increases its customary capital spending – like it did in the last decade – then that sudden extra spending does not create a correspondingly large increase in the deficit.

Why This Understates Ontario's Financial Problems

On a cash basis, we've shown Ontario is spending $20 billion more than it takes in (see the black bar for 2013, back in our second chart on page 70).

This cash number matters for two reasons. First, we pay interest on the actual cash debt. So next year, Ontario will be paying interest on $20 billion more debt, not on $11.7 billion more.

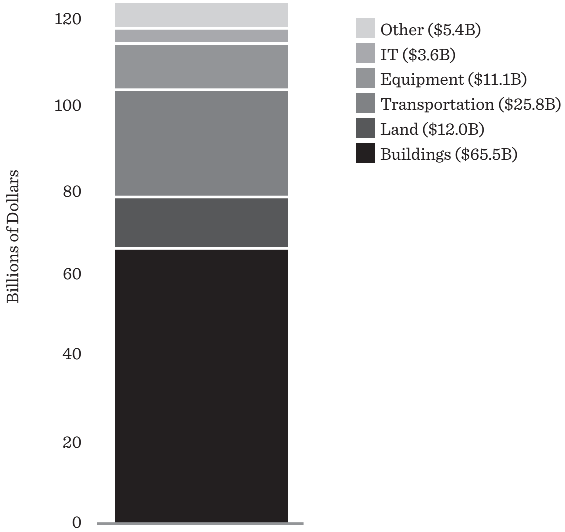
Second, even if we had an extra $11.7 billion in revenue, the situation wouldn't be sustainable – we couldn't afford to keep doing what we're doing. In the long haul, the official deficit would catch up to the cash borrowing requirement, because the amortization built into the deficit will grow (even if we forget about the extra interest cost already mentioned). We'd need an extra $20 billion a year to keep up with the current pace of spending, not an extra $11.7 billion.

In case you think that this is all in aid of constructing streetcar tracks and other infrastructure that might conceivably spur economic growth, the government helpfully provides some sobering data.

In fact, over 60% of the accumulated capital since the government started amortizing is in buildings and land. Only 21% ($26 billion out of $123 billion total) is for transportation infrastructure like roads and transit.

Of course, these investment numbers only cover what the government paid for directly; the capital investment associated with public-private partnerships like those used to construct many hospitals today is off-book, so only the annual payments affect the government's financial statements. Nearly two years ago, Infrastructure Ontario estimated that by that time it had completed $21 billion in privately-financed infrastructure (also mostly buildings), which does not show up in Ontario's capital accounts. Presumably, significantly more has been spent since then. Since the government has long-term obligations to make annual payments for this privately-financed capital, its financial situation is even more stressed than the debt increase indicates.

Accumulated Capital Investments
(Since Accounting Change, 2002)



Source: Public Accounts of Ontario 2012-2013

Structural Deficit

There is a common misconception that the current Ontario deficit is temporary because it was the result of "stimulus spending" which will soon disappear. But insofar as the so-called "stimulus" spending was on infrastructure, the startling truth is that *the stimulus spending was never in the deficit in the first place.* All that's in the deficit is the amortization of the stimulus – the mortgage payment – and that will still impact operating finances for decades to come.

Furthermore, over five years after the recession, the "infrastructure" stimulus is not just permanent, but bigger than ever, and the government is planning to keep it in place indefinitely.

> *Investments in modern infrastructure will continue. The 2013 Budget provides more than $35 billion for infrastructure investments over the next three years.*
>
> *- Ontario Budget 2013, Page xviii*

Conclusion

Ontario's debt is growing much faster than the official deficit number alone explains, and the most critical question is what to do about it. Understanding the challenge we face is essential.

The deficit we've all been taught about – the amount the debt goes up every year – is not $11.7 billion right now, but rather $20 billion. It peaked at $24 billion in 2009, and has come down only 17% since then.

The $11.7 billion deficit isn't going away on the government's current path. It wasn't caused by temporary stimulus spending, as many of us assumed, and there's a hidden pressure building under it, as the amortization of all of the ongoing capital spending increasingly hits the bottom line.

Key Questions

How much is the government planning to increase the actual net debt before its balance budget target date of March 2018?

How much will the actual net debt increase exceed the reported deficit between now and 2018? How much will the debt go up in the first year of supposedly balanced budgets?

Does the government ever plan to stop increasing the net debt?

So far in this lengthy discussion on debt and deficit, we've addressed why debt matters, the Fall Economic Statement, and our hidden deficit. If we know all of the facts that have been presented, then certainly the Liberal government knows them as well. So why do they continue to suggest they'll balance the budget by 2017-18? Is there something they know that we don't? The actual answer is "Yes", they do know more; they just haven't told us, as it's not very good news. In this Focus, I disclose Ministry of Finance and Confidential Cabinet documents that illustrate, in the government's own words, they have no way to balance the budget by 2017-18.

Confidential Advice to Cabinet: "No Plan"

In the 2013 Ontario budget, the current government went to great pains to stress that it is "on track" to balance the province's books by 2017-18. In fact, the Premier and the Finance Minister have repeated this in the Legislature and put it in writing as recently as this month.

However, there is much evidence that casts serious doubts about the validity of this claim. For instance, as raised in a previous edition of Focus, there was no mention in the 2013 Budget of the $6 billion of savings the government had previously booked from an across-the-board public sector wage freeze. There is no explanation as to whether this was still being factored into the government's planning, or conversely, if it wasn't, how the government plans to make up for that $6 billion discrepancy.

The Standing Committee on Estimates received thousands of internal documents from the Ministry of Finance and from Cabinet that confirm the government is NOT being honest about the state of the province's finances. This issue will highlight many other budget shortfalls that have been uncovered through these newly-released documents. This will prove that what the government is saying publicly about eliminating the deficit, and what they discuss internally, are two very different things.

*For 2014-15 and 2015-16, **not on track** to meet 2012 Budget deficit targets.*

– Government of Ontario (Ministry of Finance) Internal Document, March 2013

vs.

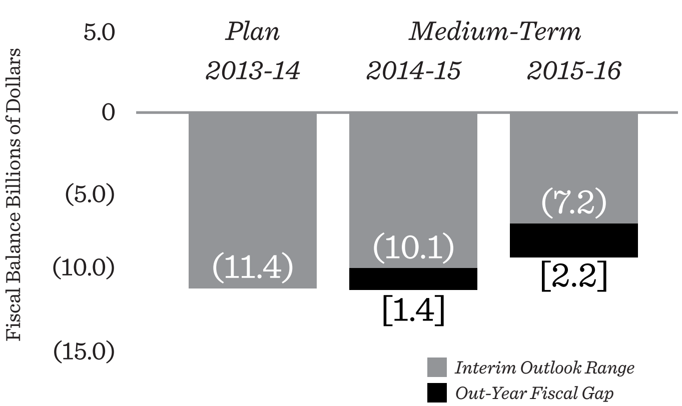
The government is on track to meet the steadily declining deficit targets outlined in the 2012 Budget and achieve a $0.5 billion surplus in 2017-18.

– Government of Ontario (Ministry of Finance) News Release, May 2, 2013.

In late February 2013, the Ministry of Finance clearly identified that the government is at least $3.5 billion off the pace needed to balance the budget by 2017-18 ($1 billion in 2014- 15, and $2.5 billion in 2015-16) (See Appendix A). It states that the "Fiscal Gap" stems from "existing ministry Results-Based Plans falling short of managing within allocations." As this chart illustrates, only two days after that assessment, the number is revised upward to $3.6 billion.

Cabinet was well aware of this $3.6 billion gap when it went on a retreat on the third week of March, 2013. But instead of taking decisive action to reduce this massive hole in their budgeting, Cabinet discussions actually resulted in an increase to the shortfall.

Out-Year Fiscal Gap



Source: Ontario Ministry of Finance, March 1, 2013

The March 24th slide deck below states the discrepancy had grown to $4.5 billion ($1.9 billion in 2014-15 and $2.6 billion in 2015-16). A document dated May 2 – the day the budget was presented – shows that the "multi-year expense plans remains largely unchanged" from a Ministry wrap-up meeting that followed. That means that the government knew when it presented its budget that this shortfall existed, yet publicly insisted they were "on track" to balancing.

It needs to be noted that the difference in the shortfall pre- and post-cabinet retreat – $900 million – is the same value of concessions offered to the Third Party in order to ensure passage of the budget (Canadian Press, May 2, 2013). It raises the question of whether the government and Third Party already had a budget deal in place in March 2013, if not earlier.

Perhaps equally troubling is the fact there are still no projections here for 2017-18. That could in fact mean the discrepancy to balance is even greater than the $4.5 billion stated in these documents.

In a previous Focus edition, we highlighted the fact that the Fall Economic Statement failed to include the medium-term outlook, breaking with tradition. This would have included tables showing how revenue, spending, and debt will look for the next three years. Now, the Finance Minister has announced he would not be presenting the Third Quarter results by the February 15 deadline as required under the Fiscal Transparency and Accountability Act, 2004. It's been several months since the government has reported real numbers or any financial details. Thanks to these newly-discovered documents, we begin to understand why.

Fiscal Outlook 2014-15 and Beyond

- No plans in place to achieve out-year deficit targets from 2012 Budget
    - Cabinet retreat outcomes that increase 2013-14 spending also add to out-year gap
    - Overall fiscal gap now at $1.9B in 2014-15 and $2.6B in 2015-16

Source: Ontario Ministry of Finance, March 24, 2013

Key Actions to Eliminate the Deficit

Commercially Sensitive Information

- Slowing growth rate of health care spending to an annual average of 2.0 per cent

Source: Ontario Ministry of Finance

On several of the versions of this slide, parts were redacted.

Key Actions to Eliminate the Deficit

- **Reducing pension expense through agreements and pension reforms**
- **No funding for incremental compensation increases for new collective agreements. Salaries for designated groups frozen until 2017-18**
- Slowing growth rate of health care spending to an annual average of 2.0 per cent

Source: Ontario Ministry of Finance

This version was not redacted, revealing there was nothing Commercially Sensitive, just politically sensitive.

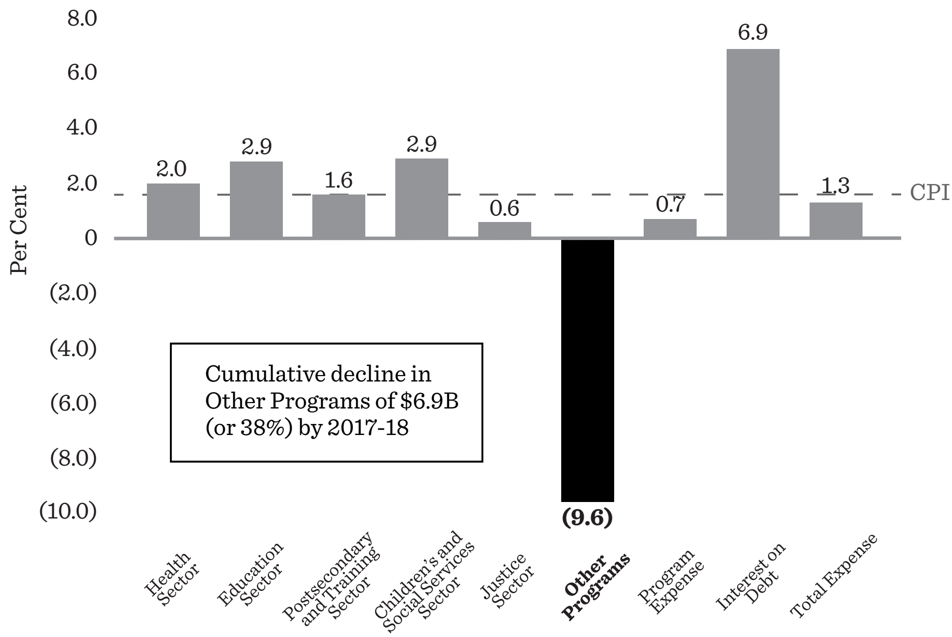
There's also another issue the government attempted to hide in these documents, but ultimately failed to do so. All mentions of public sector compensation – even the most benign mentions – were blacked out in these documents, labelling it as "Commercially Sensitive Information". However, they missed blacking-out a couple versions. By comparing the two documents above, it's clear the government was attempting to keep an important fact from the public sector unions and the public at large. The Government will need to extend public sector wage restraint past the existing two years to which it has publicly committed itself.

In another presentation prepared for cabinet shortly after the budget in early May, the gravity of the situation becomes apparent. Two scenarios for program growth expense are presented by Finance officials. They indicate that in order to reach balance, program spending reductions of $6.1 billion to $6.9 billion will be required outside of the core ministries identified (Health, Education, Post-Secondary, Justice, Social Services).

One slide ends with "Changes since 2012 Budget show a deterioration in the fiscal outlook beyond 2013-14 (based on current economic information)."

Five-Year Program Growth Scenario B

(2016-17 and 2017-18)



Source: Confidential Advice to Cabinet

The Premier's Briefing

In late January 2013, Ministry of Finance officials prepared a lengthy briefing package for whoever would be chosen as new leader and Premier.

A cover letter dated February 13, 2013 from Secretary of Cabinet Peter Wallace is addressed to "Premier" Kathleen Wynne, and three of her advisors.

In that package is an appendix which included a "Summary of Status of Key Items with Fiscal Implications." That list included the Ontario Northland divestment, LHIN reform legislation, reforms to physiotherapy services, and casino modernization.

The package included a document (below) that later triggered a further Auditor General Report. The document stated the divestment of Ontario Northland would actually cost up to $790 million; much different than the $265 million the government claimed it would save in the 2012 budget. The Auditor General confirmed in December, that in fact total divestment of Ontario Northland would cost $820 million. The sale would leave a $1.1 billion dollar gap in the budget; not proceeding with the sale will leave the $265 million savings out of the budget, plus the millions spent on the sale, to date.

That same document also refers to the government's casino modernization plan. The government had plans to establish 29 new casinos across Ontario and expected to increase Ontario Lottery and Gaming revenues by more than $1 billion a year by 2017-18 as a result. It noted two major risks to achieving that – the "potential delay in establishing a GTA casino", and the "potential relocation of slots from Woodbine Racetrack". As we now know, a GTA casino site still hasn't been selected, and may never happen, and the government has backed away from its rapid casino expansion plans. The forecasted revenue will not materialize in the 2017/18 budget.

The briefing package also lists 25 new spending items approved that weren't included in the 2012 Budget or Fall Economic Statement, and also makes mention of "non-tax revenue proposals." A separate document was made public through the investigation by the Standing Committee on Justice into the Mississauga and Oakville gas plant cancellations. This previously secret document listed nearly 50 new fee proposals the government was considering.

Item	Description
Modernizing OLG's Gaming Operations and Lottery Sales Channels (MOF)	It is expected that through implementing the OLG's modernization initiative, OLG will generate more than $600M in additional revenue between 2012-13 and 2014-15 and more than $1B per year by 2017-18. The two major risks related to achieving projected financial targets include: 1. Potential delay in establishing an interim Greater Toronto Area (GTA) casino. 2. Potential relocation of slots from Woodbine Racetrack to an alternative location.
ONTC Divestment (MNDM)	MNDM expects to incur higher than projected transition costs as part of the divestment process, which may take longer than originally proposed. The current MNDM/Infrastructure Ontario high range estimate for divestment costs is $790M. How much of these costs fall into 2013-14 and 2014-15 is not yet known.
	Source: Confidential Advice to Cabinet, January, 2013

Conclusion

The $4.5 billion shortfall uncovered in these documents provides a much more believable explanation as to why the government appears so eager to raise provincial gasoline and corporate taxes.

It also explains why the government failed to include the medium-term fiscal outlook in its 2013 Fall Economic Statement, and why the Finance Minister has elected not to report the Third Quarter results before presenting his 2014 budget.

It may also explain the recent move to change health benefit payments to retired Ontario Public Service employees after 2017.

The documents make it clear the government has no plan to balance the budget by 2017/18.

Key Questions

Why has the government insisted it is "on track" to balance the budget when Ministry of Finance documents show this isn't the case?

What steps does the government plan to take to address their $4.5 billion budget shortfall?

Does the government plan to raise taxes and/or fees to pay for this $4.5 billion shortfall? If so, which ones?

Will the government table its medium-term fiscal outlook in the 2014 budget?

Why is the government trying to hide its plans for extending public sector wage restraint from public scrutiny and from their public sector union partners?

Did the government and the Third Party already have a budget deal agreed to in March of last year, two months before its passage, that increased the fiscal shortfall to $4.5B? Is a similar deal already done for the 2014 budget?

NOTE: *A few days after this Focus on Finance was presented, the Liberal government attempted to silence me. They brought forward a Contempt motion against me in the Legislature. They claim this material contained confidential government documents and my releasing them was a breach.*

This was purely a diversion tactic by the Liberals, to have the media focus on this rather than the fact they have a $4.5 billion gap in their budget.

I fought back and within days of the false charges, the Clerk of the Estimates Committee acknowledged that all the documents I disclosed were indeed in the public domain. The Liberal 'libel chill' tactic, as it is called, failed, and the interest in my Fedeli Focus on Finance series has never been greater!

One major factor influencing the debt and deficit in Ontario is the lack of commitment to a real public sector wage freeze. The Liberals talk about it; they've even pretended to have implemented one. But as this Focus will prove, there is no across the board public sector wage freeze in Ontario.

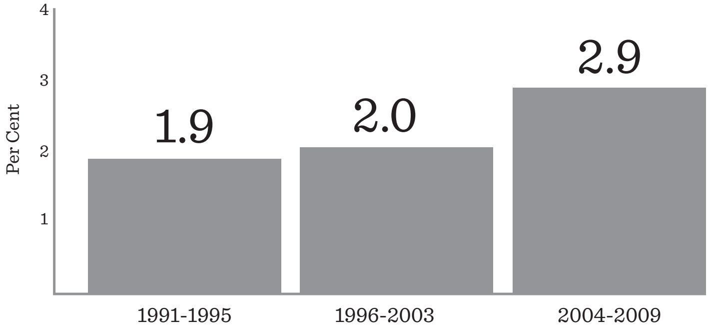
The so-called "wage freeze"

More than one million people work for one of Ontario's thousands of government employers. These range from your local school and hospital to the provincial bureaucracy, our casinos and liquor stores. So it's not surprising that salaries and benefits for government workers are the single biggest expense in the provincial budget. Controlling these costs was the primary tool the government said it would use to wrestle down Ontario's historic budget deficits by 2017-18. However, recent research – using Ministry of Labour data – reveals the government has not succeeded in freezing wages for government workers. In fact, there are hundreds of examples of deals agreed to by the government that have resulted in wage increases.

> *We can't manage the deficit without addressing what is the single biggest line in our budget – public-sector compensation.*
>
> *-Ontario Minister of Finance, July 20, 2010*

Public-sector compensation costs make up 55 cents of every dollar spent on programs. Prior to the recession the government had been exceedingly generous in handing out pay increases.

Public-Sector Settlements Average Annual Growth



Source: Presentation by Finance Minister Dwight Duncan to Ontario public-sector unions, July 20, 2010

Instead of using legislation, the government sought to achieve its pay freeze through thousands of individual negotiations. Remember – there are 4,000 collective agreements in Ontario's government sector. Seven out of every ten public employees are members of a labour union.

The 2010 budget did legislate a freeze for non-unionized employees, which it claimed would save $750 million. It was only revealed later by the Canadian Press that the government's freeze did not include things like performance bonuses, which went to 98 per cent of eligible managers.

In the 2012 budget, the government reiterated its commitment to freezing compensation, estimating this would save $6 billion over three years. (See table below.)

2012 Ontario Budget (pg 66)

TABLE 1.7 Impact of Fiscal Actions
($ Billions)

	2012-13	2013-14	2014-15	3-year impact
Expense Measures				
Expense Management Measures	(1.0)	(1.7)	(2.2)	(4.9)
Compensation Restraint	***(0.9)***	***(2.1)***	***(3.0)***	***(6.0)***
Cost Avoidance	(0.1)	(1.5)	(5.2)	(6.8)
Total Expense Measures	**(2.0)**	**(5.3)**	**(10.4)**	**(17.7)**

However, without using legislation to enforce it, the freeze was always going to be difficult to implement. Even with respect to legislation used to freeze teacher compensation – known as "Bill 115" – approximately 40 per cent of teachers continued to move through the salary grid collecting pay increases. And in an effort to repair the relationship between the current government and Ontario's teachers' unions, the premier promised elementary teachers they would receive a 2 per cent wage increase next fall without asking for concessions or offsets. According to the Globe and Mail, the deal "will cost the treasury $112 million every year."

NUMEROUS EXCEPTIONS WERE MADE TO THE GOVERNMENT'S WAGE FREEZE, INCLUDING:

MPAC: Employees at the Municipal Property Assessment Corporation received wage increases of 2.0 per cent in the first two years and 2.2 per cent in the third and fourth years.

Metrolinx: Workers at this provincial transit agency saw wage increases of 2.0 per cent in each of the first and second years and 2.3 per cent in the final year.

Ontario Medical Association: In November 2012 the government handed out a $100 million compensation increase.

LCBO: This summer employees received "signing bonuses" of roughly $1,600 per employee.

OLG Slots at Woodbine: A week after the LCBO deal, employees at OLG's Slots at Woodbine were given up to $1,200 signing bonuses over two years.

The list goes on... with exceptions to the wage freeze made for workers at:

University of Windsor
Ontario Power Generation
Niagara Parks Commission
Royal Conservatory of Music
Alcohol and Gaming Commission
Ontario Teachers Pension Plan Board
Pan Am Games Committee
Ryerson University
Elementary Teachers' Federation
Hydro One

Since a wage freeze went into effect in 2010, approximately 8 out of 10 collective agreements in the Broader Public Sector have included compensation increases. (For more information, see accompanying spreadsheet.) This figure does not include the revisions to the teacher wage freeze – "Bill 115" – made by the premier in the spring. Ontario's Auditor General is currently reviewing those costs and is expected to report back in early 2014.

A Wage Freeze is Still Necessary

The government set a target to eliminate Ontario's enormous budget shortfalls by 2017-18, but it never laid out a plan to do that.

This work was contracted out to independent economist Don Drummond, formally of TD Bank, who warned that, instead of balancing, the current plan would actually triple the province's debt to $411 billion by 2017 if the government kept spending on such a huge scale.

Even before the release of the Drummond Report, the government had been warned its fiscal plan was unlikely to balance the budget by 2017-18.

> *In past negotiated settlements, public-sector salary increases have often exceeded the inflation rate. Even after the government's announcement in 2010 that it would not fund such increases, most collective agreements negotiated since have still resulted in wage increases.*
>
> *-Auditor General, 2011*

Provincial revenue forecasts are no better than when the government said it required a wage freeze to meet its balanced-budget targets. No further expenditure restraint has been announced to offset these increases, and the government has already backed off of some of its existing plans.

Before stepping down last year, the previous premier and finance minister went so far as to draft legislation to provide a legal framework for enforcing the wage freeze, since negotiations weren't working. Entitled The Protecting Public Services Act, this 84-page piece of legislation has not been tabled by the current government. In fact, the 2013 budget removed all references to a wage freeze and instead proposed to "work together" to achieve desired outcomes.

Rather than a wage freeze, per se, the finance minister now says the government will "advocate for wage constraint," refuses to use the term "wage freeze," and appears to be explicitly backing away from the policy of his predecessor.

Then:

Where collective agreements cannot be negotiated that are consistent with the fiscal plan… the government will consider all options to meet its fiscal goals, including intervention through legislation or other means.

-Budget 2012

Now:

We're working closely with the stakeholders involved to administer negotiations within the pay envelope that we now have.

-Ontario Minister of Finance, September 2013

Conclusion

Ontario has a serious problem, and the government is not being honest about it.

Key Questions

If the government's wage freeze has failed, does the province's fiscal plan still include the estimated $6-billion savings from this measure?

If the government's wage freeze has failed, does it still expect to balance the budget by 2017-18?

We've already covered some of the additional sources of revenue the government has been using to attempt to balance the budget. Sources such as Federal Equalization payments of over $10 billion, received since becoming a 'have-not' province, come to mind. In this Focus you will discover a shocking source of revenue that took almost 10 years to come to light.

No Plan to Retire the "Debt Retirement Charge"

In his 2011 annual report, former Ontario Auditor General Jim McCarter noted that the provincial government had not provided the public a full accounting on the status of the Debt Retirement Charge (DRC) for some time, even though it was required to do so by law.

McCarter noted in his report that the original amount of debt, which the DRC was intended to pay off, was $7.8 billion, yet there was still a balance, even though the current government had collected $8.7 billion by March 31, 2011. Surprisingly, the government now claims that it still owed $5.8 billion as of that date!

The original $7.8 billion figure was established in 1999 during the restructuring of the province's former electricity utility, Ontario Hydro, and was never subsequently challenged by the current government until difficult questions started to be asked. We have now discovered the government had re-set the debt to $11.9 billion, a secret it kept to itself from 2004 until after the 2011 election.

More Questions than Answers Remain

The most recent annual report from newly-appointed Auditor General Bonnie Lysyk states the amount collected has since grown to $10.6 billion as of last year, while the government claims $3.9 billion is still owed and refuses to say specifically when it will be fully paid off. Ontario households and employers can be forgiven for scratching their heads and wondering why this surcharge remains on their monthly electricity bills, where all of this money has really gone, and what is the plan for ending it.

> *Section 85 (of the Electricity Act, 1998) requires that the Minister of Finance "from time to time" determine the amount of the outstanding residual stranded debt and make this determination public.*
>
> *-Office of the Auditor General of Ontario, 2011 Annual Report, page 12*

A Little History

In 2002, Ontario families and employers began paying a specific surcharge on their monthly electricity bills in order to pay back debts accumulated by the former Ontario Hydro. The amount of that debt was $7.8 billion, and it was estimated that by 2012 enough money would be collected to meet these obligations. The DRC is applied at a rate of 0.7 cents per kilowatt hour (kWh). With average residential use ranging between 800 kWh and 1,000 kWh per month, this equates to between $5.60 and $7.00 on an average monthly bill. Beginning in 2010, the government applied the Harmonized Sales Tax to the DRC. In total, the DRC raises close to $1 billion a year in annual revenue.

As 2012 approached, the government pushed back the estimated date for paying off the residual stranded debt from 2012 to "somewhere between 2015 and 2018." In the most recent annual report from the agency in charge – the Ontario Electricity Financial Corporation (OEFC) – even this date range was omitted. Why? (Source: Ontario Electricity Financial Corporation, Annual Report, 2012)

After the Auditor General pointed out in 2011 the government's failure to comply with its reporting requirements, the Ministry of Finance provided a long-awaited update on the Debt Retirement Charge on May 15, 2012. It stated the remaining residual stranded debt was $4.5 billion, leading to numerous questions, such as how was it possible to collect $8.7 billion and only pay down $3.3 billion worth of debt? The government claimed that there was interest owed on the debt, even though the definition of the residual stranded debt and DRC, as written into law, does not include interest payments: "the definition of residual stranded debt in section 85 [of the Electricity Act] does not include interest or other [Ontario Electricity Financial Corporation] expenses." (Source: Office of the Auditor General of Ontario, 2011 Annual Report, page 125)

This, of course, begs the question – where did this money go and why are we still paying the DRC?

Yearly Revenues from the Ontario Debt Retirement Charge

(2002 to Present)

2013-14:	**$957 million** *(2013 Budget projection)*
2012-13:	**$957 million** *(2013 Budget interim figure)*
2011-12:	**$952 million**
2010-11:	**$944 million**
2009-10:	**$907 million**
2008-09:	**$970 million**
2007-08:	**$982 million**
2006-07:	**$991 million**
2005-06:	**$1.021 billion**
2004-05:	**$997 million**
2003-04:	**$1.0 billion**
2002-03:	**$889 million**

TOTAL **$11.6 BILLION**

Ontario Ministry of Finance on August 18, 2011:
Amount of debt to be paid off = $7.8 billion

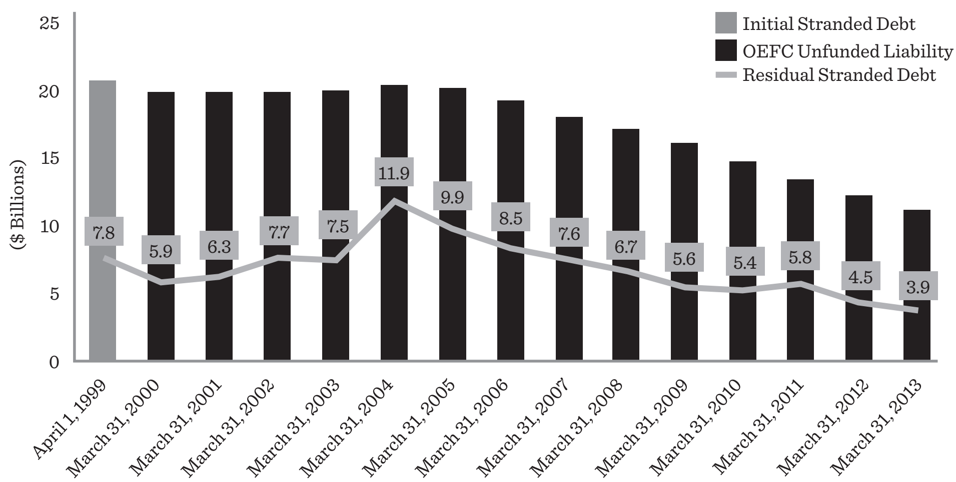
Ontario Ministry of Finance on May 15, 2012:
Amount of debt to be paid off = $11.9 billion

-Ontario Electricity Financial Corporation, Annual Report 2010-11, released August 18, 2011; and, Ontario Ministry of Finance, press release, May 15, 2012

The $4 Billion Question

The most curious aspect of the government's update in 2012 was the fact it retroactively restated the 2004 amount of residual stranded debt as $11.9 billion – a $4.1 billion increase from the original amount. However, a review of the 2004 annual report from the Ontario Electricity Financing Corporation makes no mention of this sudden increase. In fact, neither does any annual report up to the 2011 election. The figure used was $7.8 billion in 11 consecutive annual reports. In essence, it was like a credit card bill we kept paying, but no one ever told us how much was left. When that number was finally revealed, the original balance jumped $4 billion.

Residual Stranded Debt Since April 1, 1999



Note: Unfunded Liability amounts are from OEFC Annual Reports from 1999-00 to 2012, and the Annual Financial Statements for 2013.
Sources: Residual Stranded Debt value for April 1, 1999, as announced on April 1, 1999. Values for the period from March 31, 2000, to March 31, 2010, as estimated by the Ontario Ministry of Finance in the *2012 Budget* and for March 31, 2011, to March 31, 2013, as determined by the Minister of Finance in accordance with a regulation made under the *Electricy Act*, 1998.

Where did all this money go if it wasn't paying off $7.8 billion of residual stranded debt? The auditor gave one major clue in his 2011 annual report:

"External legal advisers we engaged to assist us ... confirmed our view that section 85 of the Electricity Act, 1998, which is titled 'The Residual Stranded Debt and the Debt Retirement Charge', allows the DRC to be used for any purpose that is in accordance with [the government's] objectives and purposes, and not just the retirement of the residual stranded debt." (Source: Office of the Auditor General of Ontario, 2011 Annual Report, page 12)

While it appears the current government clearly exploited this loophole, it is nevertheless a loophole.

When originally implementing the DRC, the Minister of Energy of the former government said explicitly it was the government's policy that: "All revenues from the DRC will go directly to the Ontario Electricity Financial Corporation to be used exclusively to service the residual stranded debt. Once the residual stranded debt has been retired, the DRC will end." (Source: Office of the Auditor General of Ontario, 2011 Annual Report, page 124)

It was therefore a deliberate change in government policy not to use separate accounting to track the residual stranded debt. In a 2011 briefing to the Ontario PC Caucus, government officials confirmed that they combine revenues collected through the DRC revenues with other electricity-related revenue streams, which are then all applied together to the overall unfunded liability. The amount of remaining residual stranded debt is then recalculated, each year, to derive a remaining balance.

What's Really Going on Here?

Two things – first, the Debt Retirement Charge is not earmarked toward the residual stranded debt, even though that is its intended purpose. Second, the government really has no plan to ever eliminate the DRC. Take a second look at the figure above. Between 2010 and 2011, the amount of debt owed actually increased from $5.4 billion to $5.8 billion – over the same period the government raised $950 million in DRC revenues.

Is it any wonder the government cannot present its long-term plan to eliminate the DRC?

The most recent government update on the remaining residual stranded debt figure came in the 2013 Fall Economic Statement at $3.9 billion – which, coincidentally, is roughly the difference between the original estimate and government's revised estimate for 2004.

Conclusion

If the government had properly managed the electricity system and directed money collected through the DRC toward its intended purpose, the residual stranded debt should have been paid off by now, and the charge should have come off Ontario electricity bills. Instead, it appears that when the government needed money for other expenses, it diverted these funds toward those purposes, prolonging the amount of time Ontario families and employers will be required to pay the DRC.

Key Questions

If the government has collected roughly $1 billion in DRC revenues every year for the past 12 years, why is it not able to give a specific date for when the residual stranded debt will be paid off?

How does the government explain the fact that it used $7.8 billion for the amount of debt each and every year for 8 years, only to revise this estimate upwards to $11.9 billion immediately following the 2011 election?
I started out talking to you about what every MPP hears throughout our travels:

MY
FINAL
THOUGHTS

I started out talking to you about what every MPP hears throughout our travels: skyrocketing energy rates, new taxes, and crushing red tape. From there you were provided considerable evidence that the finances in Ontario are far worse than the government has disclosed, and even amongst themselves, the Liberals acknowledge they have no plan to balance the budget.

Let me conclude by saying there is a very disturbing scenario playing out right now. The Liberals have been hiding any real numbers.

In October 2013, Finance Minister Charles Sousa failed to deliver the long-range assessment of Ontario's fiscal environment, as he was obligated to do, under the Fiscal Transparency and Accountability Act.

Here is what I asked him during Question Period: "Minister, The Fiscal Transparency and Accountability Act states, "Within two years after each provincial election, the minister shall release a long-range assessment of Ontario's fiscal environment." Minister, you're two weeks late. When will you be releasing this assessment that you were legally required to release?"

Minister Sousa responded: "We have a Fall Economic Statement that's coming out shortly. We've produced first-quarter results that achieve our opportunities and that show the success we've had to date."

So he'll show us the numbers in the Fall Economic Statement! However, when it came out, there were no Medium-Term Outlook numbers included. In addition, individual ministry expense numbers were not listed for 2016-2017 – just the Total Program spending – which magically falls in 2017 to balance the budget. Still no numbers!

Then in February, 2014, the Minister announced he would not be presenting their 3rd Quarter Results on February 15; as is also required under the Fiscal Transparency and Accountability Act.

The government is hiding the truth, because any one of these three sets of figures would demonstrate the province is not on track to balancing the budget by 2017-18.

I continue to ask important finance questions almost every day during Question Period. Sadly, this government will not take that opportunity to set the record straight or to tell us what their plan for Ontario is.

They continue to tell the Legislature, the financial community, and the public one thing, while their own once-secret documents prove they know the complete opposite to be true.

Companies continue to leave Ontario. And the Liberals continue to introduce new taxes.

Lately, the government has taken to deflecting any concern you may have about their finances, by talking about selling beer and wine in grocery stores, or selling parts of Hydro One. These are purely intended for two reasons: to have you debating those issues rather than looking at the real issue of debt and deficit, and to use any new-found revenue to reduce the deficit.

They continue to tell us that they will put revenue from the sale of assets into the newly-created Trillium Trust. But we caught the Liberals red-handed during the Budget deliberations. The Act states the government 'may' put a 'portion' of any asset sale into the Trust. We brought Amendments forward to change 'may' to 'must' and 'portion' to 'all'. After all, if the intent was to put all the money into the Trillium Trust, then say so. But the Liberals voted the Amendments down – meaning they are now free to put any revenue from the sale of an asset right into general revenue, and apply it against the deficit.

As a final push, we proposed an Amendment, "Within 90 days of the sale of an asset, the Auditor General report to the Legislature on what was sold, how much was received, and where the money went". That's pretty simple, isn't it? Yet again, the Liberals voted down the Amendment. So much for being "open and transparent".

Closer inspection of the Budget revealed the full story. Asset sales are included in the "other non-tax revenue" table. And page 232 of the Budget is quite revealing, showing asset sales of $900 million this year and $1 billion next year. Almost $2 billion in asset sales have already been booked and built into the budget – and these assets have yet to be sold. So much for putting the money into the Trillium Trust, as promised – and now we know why the Liberals voted against our three Amendments.

John Ivison said it best in his National Post column when he wrote, "Too bad Charles Sousa, the province's finance minister, had already fluffed the books for this year and next with net revenue gains from "asset optimization" totaling $2 billion".

Yes, it is indeed too bad the Liberals have fluffed the books. As a result, we will be paying for their mismanagement for generations to come.

If you would like to download previous editions of Fedeli Focus on Finance, please go to **www.Fedeli.com** and click on the 'your MPP at work' link.

In addition, if you would like to receive future editions of Focus, go to **www.Fedeli.com** and type your address in the subscription box on the front page.

Victor Fedeli is a life-long entrepreneur, specializing in communications.

In 1989, his Fedeli Corporation was named 34th in the 50 Best Places to Work in Canada.

In 2003, he successfully ran for Mayor of the City of North Bay, and served two terms.

On October 6, 2011 Vic was elected MPP for Nipissing. Within a month, he was named as the Ontario PC Energy Critic. After serving two years, he was named PC Finance Critic.

In this new role, Vic began publishing Fedeli Focus on Finance, a monthly series of financial newsletters, which as the names suggests, offers an in-depth look at the finances of Ontario.

His shocking revelations – through internal government documents kept secret by the Liberals until revealed through exhaustive research by the Ontario PC Party – are what prompted this publication.

Victor Fedeli
MPP, Nipissing
PC Finance Critic