FOCUS ON FINANCE 5

A LOOK INTO ONTARIO'S FINANCES

VICTOR FEDELI, MPP
INTERIM LEADER OF THE OFFICIAL OPPOSITION

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About the cover

If this book had a formal title, it would be *House of Cards*, because that is what the government has created. The Auditor General will use words such as “bogus” or “unreliable” and “significantly misstated” to describe Ontario’s finances. The Financial Accountability Office says the government uses “unlikely assumptions” and that their “broader pattern of secrecy” makes it “difficult to assess the plausibility” of the government’s financial projections. Ontario is the truest example of a *House of Cards*.

PREFACE

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Over the past five years, I have written and distributed 60 of my monthly *Fedeli Focus on Finance* newsletters and this is the 5th annual *Focus on Finance* book. They have all been non-partisan. Yes, they may be caustic at times, but there are no political Parties mentioned, and they have proven to be fair and balanced. And for those who have been regular followers, you know that you "heard it here first" on many occasions.

In 2015 we first exposed that the revenue from the sale of Hydro One was not being used to pay for infrastructure, as the government outlined. There was one line in the 167-page finance Bill that allowed them to use the revenue to reimburse the Crown for past expenditures. It was the final piece in the fire sale of Hydro One that allowed the government to record the proceeds in Operating Revenue, to artificially reduce the deficit and attempt to balance the budget. In fact, the scheme worked so well that the government used exactly the same line in manipulating the cap-and-trade tax revenue to perform the very same function, in the very same way.

In 2016 we broke the Samsung story, where readers saw Ministry of Energy documents detailing how the government could have got out of $5.2 billion in energy contracts, at no cost. These documents were part of the 300,000 Gas Plant Scandal Hearing documents the opposition parties eventually recovered. For the most part, they were marked as Confidential Cabinet documents. They proved to be a window into the inner-workings of the government, who never would have imagined they would see the light of day. While much was shared with the public, the Samsung story was by far the single-largest revelation, outside of the Gas Plant Scandal and subsequent cover-up. (More on that later).

Over the course of last year, we proved that the so-called Fair Hydro Plan was nothing more than financial engineering and the government's talking points were all based on opinion polls, not on actual statistics or any facts. We first revealed that Ontario Power Generation was co-opted into being the financing arm of the government's scheme – a fact borne-out by the Auditor General, who this year announced that using OPG would cost the taxpayers a further $4 billion.

This year, our focus really is on finance, and we will guide you through Ontario's house of cards. There were plenty of revelations regarding the state of Ontario's finances over the last 15 months. The Legislature's independent officers, the Office of the Auditor General and the Financial Accountability Office, were both prolific. They provided a steady flow of commentaries as well as annual and special reports, particularly pertaining to Ontario's hydro sector.

We'll start off, as I do most years, by debunking much of what the government Ministers said in public. Then we'll take a 15-month tour through the stories that had significant impact on the state of Ontario's finances. That will comprise most of the book – and really paint a complete picture for you. This will be followed by a re-cap of the Gas Plant Scandal – as that dark chapter in Ontario has finally reached its end.

I really hope you enjoy this edition and find it to be fair and balanced – and very revealing.

Thanks for reading and for supporting my *Focus* series!

JUST THE FACTS

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This past year has been one for the record books. The disturbing trend of ministers saying one thing when the polar opposite is true, has unfortunately continued. They do it shamelessly, as the examples later in this chapter will point out. And the Legislative Officers continue to provide detailed accounts of the true state of Ontario's finances, while the government continues to disparage them. We'll begin there.

Early last year, Ontario's Financial Accountability Office (FAO) warned of the government's "broader pattern" of secrecy and that their refusal to provide information was making it "difficult to assess the plausibility of the government's financial projections." Not a good start to the year. This was quickly followed by the government continuing to ignore the ruling of the Auditor General (AG) regarding the booking of pension plan surpluses as an asset. AG Bonnie Lysyk says she won't give her "seal of approval". This is no small dispute, as more than $11 billion dollars are what's at stake, and could easily tip the province into the black and lower the province's debt.

Last spring, the government was so eager to spread the word about their so-called Fair Hydro Plan, that they bought $1 million worth of taxpayer-paid advertising. The Auditor General weighed in calling the ads a "pat-on-the-back" and could be considered partisan. She also said the ads likely wouldn't have been approved under old government advertising rules. The Auditor was so incensed by the changes that she penned a Special Report to the Legislature decrying the changes. She said changing the rules would end up giving taxpayers the bill for millions of dollars of partisan ads. "Sure enough, the government walked right through that open door," she added.

It seemed to head straight downhill from there. Responding to the government's Economic and Fiscal Outlook, "the FAO projects a steady deterioration in Ontario's budget deficits due to moderating revenue growth combined with higher expenses" and "Beyond 2017-18, the deficit is projected to deteriorate steadily due to rising expenses and slower revenue growth."

This brings me to an interesting point. The government's 2018 Budget shows the province plunging into deficit and remaining there for the next several years. The Premier stated repeatedly that this is a "conscious choice" they made … to invest in Ontario. But the FAO had forecast this, as the one-time revenues the government had artificially balanced their budget with, would no longer be available. The FAO said last year's budget benefitted from "a $3 billion boost in one-time non-tax revenues." He describes these as "temporary revenues" and include "an increase in federal transfers for infrastructure, additional sales of public assets, including the recent sale of Hydro One, and additional one-time cap-and-trade proceeds." He warns "However, beginning next year, the growth in tax revenues is projected to be moderate, while the boost from one-time non-tax revenues will end." So, while the government claims these new deficits are designed to help families, the FAO had forecast last year that this was inevitable. Plunging us into deficit was not a conscious choice … it's a consequence of using one-time revenue!

Next, the Financial Accountability Office honed in on the government's so-called Fair Hydro Plan. It was very revealing to see the FAO state, "Due to the nature of the proposed financing transaction, (involving OPG) the FAO recommends that Members of Provincial Parliament obtain assurance from the Auditor General that the province's proposed accounting treatment for the electricity cost refinancing meets public sector accounting standards and will not impact the province's annual surplus/deficit and net debt." That set the table for the Auditor General, who announced "the government plans to borrow about $26 billion … but it does not want to reflect the overall impact of these borrowings on the consolidated financial statements." The AG acknowledged, as did the FAO, that the government planned to "record anticipated revenue as an asset to offset borrowings." As a result of attempting to use OPG to bury the true costs, this will falsely show "no impact on the net debt." The Auditor then repeated, three different times, "this is NOT allowed under Canadian public-sector accounting standards." She added that "keeping the borrowing off the province's books is a "dangerous precedent" and a move that "does not meet public sector accounting standards."

Beginning in the fall and into the spring of 2018, the comments from the Legislative Officers were more stinging. The FAO released two reports where the titles explained it all. *Optimistic Revenue Projection Underpins Government’s Balanced Budget Plan* and *Debt Reduction Commitment Based on Unlikely Assumptions* revealed a steadily-deteriorating deficit. In a third report on the Economic and Fiscal Outlook, the FAO concludes “It is becoming more difficult for legislators and the public to assess the government’s fiscal projections. This has reduced the transparency and reliability of Ontario’s fiscal plan.” The AG issued her own report, *Ontario Government Understates Annual Deficit and Net Debt*, where as per last year, she issued a ***qualified*** audit opinion. She said the “statements significantly understated the 2016-17 deficit, as well as the province’s net debt.” The AG announced the 2016-17 deficit was understated by $1.44 billion and the net debt understated by $12.4 billion. She closed with two more scathing comments. “The Legislature and all Ontarians must be able to rely on the province’s consolidated financial statements to fairly report the fiscal results for the year. This year they cannot do so” and “the government inappropriately recorded the market account of the Independent Electricity System Operator.” Unlikely assumptions. Significantly misstated. Can it get any worse than that?

The Auditor issued a further report on the hydro scheme, entitled *Concerns About Fiscal Transparency, Accountability, and Value for Money*. The AG opened with, “The government’s structure will hide from Ontarians the real financial impacts of its electricity rate reduction.” She then stated, “When governments pass legislation to make their own accounting rules that serve to obfuscate the impact of their financial decision, their financial statements become unreliable.” AG Bonnie Lysyk felt it her “responsibility to speak out when the financial information of the government is not, or will not be, presented fairly and transparently to both the Legislature and Ontarians.” She said the government’s intention was to “avoid showing a deficit in the province’s budgets and consolidated financial statements, and to likewise show no increase in the provincial net debt.” The AG concluded “the government did not properly account for this debt … and is not planning to account for it properly.”

The FAO became even more concerned that there is reduced transparency and reliability of Ontario's fiscal plans. It projected a "significant increase in the budget deficit due to the loss of time-limited revenue" and that this is a "significant deterioration since the spring outlook and is primarily the result of the introduction of the Fair Hydro Plan." Because the government's numbers do not include cost of the hydro scheme but do include the pension funds (neither being acceptable to the AG), they conclude "It is becoming more difficult for legislators and the public to assess the government's fiscal projections. This has reduced the transparency and reliability of Ontario's fiscal plan."

Again, the title says it all in the Public Accounts section of the AG's Annual Report: *Government Financial Statements Becoming Increasingly Unreliable*. The government's continued use of nonstandard accounting could throw off the accuracy of the province's bottom line by up to $4.5 billion next year, according to the Auditor General. "There is a very real risk that the balanced books expected to be reported by the government using these accounting methods next year will conceal the true annual deficits and net debt." "This will seriously distort the true state of the province's finances."

The Auditor General saved her most shocking comments for her audit of the Independent Electricity Sector Operator (IESO) as it pertains to the accounting methods used for the government's hydro scheme. The Auditor has said she thinks "the accounting is bogus," and highlights the fact that the financial and accounting structure was designed to avoid reporting the hydro scheme's costs. She claims it was "allowing the government to falsely claim" their budget numbers. The Auditor's concerns also included "incorrect accounting, deceptive and obstructive behaviour by the IESO's board and management, and poor financial controls." It's so bad, the Auditor General warned that if the improper accounting isn't fixed, she might issue an ***adverse*** opinion on Ontario's books. That would be a first in Canadian history for any government's financial statements!

Just take a moment to glance back at the last few pages and review the underlined words; all quotes from the Legislative Officers. They reveal a very serious pattern of deceit. That alone should keep you up at night.

While the Legislative Officers were sharing their alarming concerns with the public, the government and its ministers were spinning a very different story. Last year's *Focus* opened with a few tall tales from various ministers. This year, there are even more to choose from, and I will share a few choice selections.

The Finance Minister tops the list, as he repeats these same alternate facts over and over and has other cabinet ministers and MPPs repeating them as facts. It's actually gotten to the point where these phrases roll of their tongues so easily, to the point I think the government MPPs actually believe what they're saying. Here is what the minister claimed on one TV program alone. He stated the government has "slayed the deficit" and "balanced the books", was "projecting 140,000 (new) jobs every year", "we are the top foreign direct investment" destination, and Ontario's "debt-to-GDP remains the same and will be tapering down". Not one of those statements is even remotely true. In fact, the polar opposite would be closer to the truth, and I respond to each of these much later in the book.

The former President of the Treasury Board was also on TV talking about Ontario's debt-to-GDP. She stated, "We watch that debt-to-GDP ratio very, very closely. The number 40 is the magic number. If you exceed 40% of your GDP you're in territory you don't want to be in. And we're below that and we will stay below that. And we will continue to reduce the debt-to-GDP ratio. That is fiscal responsibility." All admirable statements – but again – not true! Ontario's debt-to-GDP is up by half a percent, from 37.1% to 37.6% this year. And it's not reducing – it is forecast to rise to 38.2% in 2019-20 and to 38.6% the year after. While I listened to her, the light came on! Now I realize why they needed to break accounting rules and add the pension fund's surplus onto the government's books, and put the billions of expenses of the hydro scheme over onto Ontario Power Generation's books. If that did not happen, Ontario's actual debt-to-GDP would have to be listed at over 40% – over the magic number, and into "territory you don't want to be in." Their motives are clear as a bell.

Meanwhile, the Labour Minister stood in the Legislature and announced "It's true that the Ontario economy is doing very well; manufacturing exports are up." Except that isn't accurate. A recent headline, "July Trade Deteriorates", leads the story indicating

Ontario's exports fell 22% last summer. Then the Minister doubled-down with, "We're leading the G7 in economic growth." Ontario's Finance Minister backed him up with "Ontario is number one in North America when it comes to growth." Except neither of those statements are even close to being accurate. Ontario's growth is not number one; it is tied for 28th place – there are 27 U.S. states ahead of us!

There were a few one-hit wonders as well. One gaffe-prone MPP boasted about his government tripling the provincial debt. "We have tripled (the debt) and we're proud of it ... I would do it again and I would do it proudly." When it was reported in print, he denied ever making the statement. In fact, he then spent the weekend on talk radio claiming he never made such comments, and sponsored Facebook ads claiming the article was false. That is until the newspaper aired the taped recording of the MPP's statement. It was only then that the MPP issued an apology, and admitted the entire conversation was indeed printed word-for-word.

A former cabinet minister stated that "All political parties are by law required to present a full costing of their election platform" and suggested that any Party that doesn't would knowingly and deliberately break the law. Even though the statement was Tweeted by the coms folks in the Premier's office, it is untrue. Apologies were issued by all government officials involved.

Another former cabinet minister was attempting to placate the business community who were asking the government what they intended to do about the dramatic U.S. tax cuts and their effect on Ontario businesses. The then-minister said the Ontario government is prepared to lower corporate taxes to keep the province competitive with the U.S. He added that a competitive edge is important to Ontario's economy and he wants to assure the business community the government intends to maintain it. Sadly, in the 2018 budget, the government added $2 billion in new taxes affecting 1.8 million individuals and tens-of-thousands of businesses.

Perhaps the most egregious offence centered around the accounting treatment of the so-called Fair Hydro Plan. Recall that the Auditor General called the accounting a "dangerous precedent" and a move that "does not meet public sector accounting standards." To defend the government, the Energy Minister stood in the Legislature and insisted "KPMG and Deloitte worked on the accounting related to the Fair Hydro Plan. They ensured that this plan was in accordance with public sector accounting." This was repeated in many variations over a five-month period. That is, until the Auditor General wrote to the Public Accounts Committee. "Deloitte and Ernst & Young have confirmed to us that they provided no formal opinions approving the accounting for the Fair Hydro Plan." She also wrote, "KPMG told us that it has not provided an opinion on the accounting for the Fair Hydro Plan." With this kind of blatant defensive action coming from the government, how can you ever believe anything they say?

This chapter ends with a clear example showing that the government does not want anyone to have information where they lose control of the message. In May 2017, the government made an announcement regarding small business tax reforms, and I asked both the Minister Responsible for Small Business and the Minister of Economic Development for proof to back up their claim. I did this on June 1, by tabling an Order Paper Question. Each Opposition MPP has the opportunity to present 10 of these questions at any time, and there is a prescribed 24-day response time by the government. Finally, at the end of October, both ministers responded by telling me I should re-table my question to the Minister of Finance, which I reluctantly did. Six weeks later that minister replied and re-directed me back to the first Minister of Economic Development. Talk about a runaround! After a complaint to the Speaker and a written admonishment from him to the Government House Leader, I finally received a response in February, albeit an evasive one. A simple question shouldn't take over seven months to receive a non-answer. It doesn't get more cynical than that.

HOUSE OF CARDS

HOUSE OF CARDS

This next chapter (which is about 3/4 of the entire book) will take you on a chronological review of the events affecting Ontario's finances, from January 2017 through to the 2018 budget.

January 2017 – Happy New Year, anyway

After the champagne corks were all swept up, and the revellers headed home, the first morning of 2017 presented a stark reality: life just got more expensive in Ontario.

If you stopped at the gas pumps that first morning, you would have found the price of gasoline rose by 4.3 cents/litre. The government first claimed that the cost of cap-and-trade per household would be $156/year, including an increase in gasoline costs of $8/month. But once their phones started ringing, they came up with a new line. "Any costs associated with fighting climate change are borne by fuel distributors who decide how and if the costs are passed on to consumers." So now "it's not us … it's them!" The government also claimed that home heating fuel would go up by $5/month, but the Ontario Energy Board (who won't allow the companies to list the cap-and-trade charge separately on the bills) stated it will be up to 34% higher than the government's claim.

Not only is the price not stated separately on any energy bill, there really is no way of knowing how much extra you're paying for groceries, clothes, hardware, sporting goods, or any other goods and services you buy. After buying carbon credits, businesses then pass along their increased costs to the end consumers, but there is no transparency, so you will never know the true cost of the cap-and-trade tax.

I started the year off at the Economic Club's annual Outlook breakfast, where the five major banks' chief economists spoke. RBC's Craig Wright stated that any carbon tax should be revenue neutral – that is return all the revenue to families to cope with the higher cost of living it causes. He followed this up with a deputation to the Legislature's all-Party pre-budget consultations and stated, "What I typically think of successful carbon pricing agreements is that they have to be transparent, predictable, and gradual and, most importantly, they have to be revenue-neutral. The issue is that carbon pricing is to change the structure of the economy; it's not about growing the size of government, and that's when you get into this revenue neutral side. If it's just about the government grabbing more money and then reallocating it, that's less than ideal, especially in the context of a more competitive environment."

Sadly, in Ontario, this program has absolutely nothing to do with reducing greenhouse gas emissions; it's all about a revenue grab. Here's how this happens.

In *Focus on Finance 4* we revealed the government was using cap-and-trade to pay for already-budgeted items and using those previously-earmarked funds to artificially lower the deficit. Schedule 68 of the budget allowed this to happen through Subsection 3. It allowed the government "**To reimburse the Crown for expenditures incurred by the Crown, for any purpose described in paragraph 2**". This includes transportation infrastructure; public transit vehicles; technologies, infrastructure, vehicles, buildings, and structures that reduce greenhouse gas emissions associated with the movement of goods. All previously-budgeted items! This concern was then shared by the Financial Accountability Officer, who appeared at the Cap-and-Trade Committee Hearings and addressed his concerns about Section 68. The true intentions were also laid bare first in the Fall Economic Statement and then the 2016 Budget, where cap-and-trade proceeds were entered directly into general revenue.

Finally, the Auditor General weighed in with "Ontario's cap-and-trade will not significantly lower emissions within the province by 2020". The Ministry's own study projected that Ontario will achieve less than 20% of the reductions required to meet the province's 2020 target. They plan to count emission reductions achieved in California and Quebec, using allowances purchased by Ontario emitters, to meet the remaining 80% of the target. The Auditor concluded the funds for those purchases "may be leaving the Ontario economy for no purpose other than to help the government claim it has met a target."
Ontario families already struggle to pay some of the highest hydro bills and taxes in the country, yet the cap-and-trade scheme is adding costs onto everything from gas to groceries. A revenue neutral plan could mean a refund on your hydro bill or a cut on

income taxes. The plan would also reduce emissions here at home, while putting money back into the pockets of Ontario families.

January also saw the release of a pair of reports that were of concern. The Ministry of Finance released *Ontario's Economic Accounts*, which noted that business investment in the province declined by 0.8%, including a drop of nearly 6% in investments in machinery and equipment. In addition, the Financial Accountability Officer released a report that notes Ontario has experienced a decrease in the share of both full-time and private sector positions, and the "employment rate remains well below pre-recession levels." The FAO also found that employment prospects for youth remain stagnant, with unemployment rates of nearly 15%; well above the national average. These are on top of the earlier news that Ontario's foreign direct investment has dropped from 1st to 4th place in North America; from $7 billion to just $4 billion. Ontario's market share has been cut in half from 12% in 2015 to just 6% last year.

As has been the case month after month, hydro still dominates the discussions. In writing about the all-Party pre-budget consultations, I've mentioned Craig Wright's comments on cap-and-trade. He also weighed in on the hydro rate crisis, telling the committee "I think electricity is one of the many areas that makes Ontario investment less attractive than only a short while ago." He was backed up by many vocal groups, including Rory McAlpine, a Sr. VP with Maple Leaf Foods who told the committee "our electricity price increased by 18% in 2016 ... I think anyone would agree that 18% is a large increase." He added, "If we had operated in Manitoba instead of Ontario it would have been a 65% saving on our electricity bill."

Norm Beal, CEO of Food and Beverage Ontario also weighed-in on skyrocketing electricity prices. He said he's hearing from his members who receive daily calls from U.S. jurisdictions asking them to relocate for cheaper hydro. His members are telling him "We've had enough. We're starting to look at the alternatives south of the border." Gerry Macartney, CEO of the London Chamber of Commerce, said "Many decisions are being made because of the high cost of electricity, and companies are looking at other, more competitive jurisdictions." Frank Dottori, CEO of White River Forest Products, summarized the feelings of most deputants; "Most jurisdictions use energy costs to promote economic development, not to kill jobs, which is what we're doing in Ontario."

You'll need to pull even more money out of your wallet for the myriad of fees that came into effect this month. If you drive a car – you'll pay more. If you heat your home with gas – you'll pay more. If you camp, fish, or hunt – you'll pay more. We're not talking chump change here – vehicle and driver registration fees have increased by more than $500 million over the last four years. In fact, service fees will cost families $2.74 billion this year, up by nearly 40% in just five years.

There is also a series of regulations that went into effect. Restaurant chains with 20 or more locations must start posting caloric content on their menus. After seeing this at the Quorum Restaurant here at Queen's Park, I've nixed my daily Caesar salads for lunch! Travel agents and wholesalers must include the all-in price in their advertising. Towing companies must now post their rates on their trucks, must accept credit cards, and cannot demand cash. Spousal and child support will no longer be treated as income for people receiving social assistance or those on ODSP, which will end the claw-back from this. And the maximum cost of a $100 payday loan will drop to $18 from $21.

The month ended with a story close to home. Back in October 2016, the Premier announced Ontario will be buying $70 million of water-power-produced electricity from Quebec Hydro. The government boasted that they signed a deal for Ontario to import up to two terawatt hours of electricity annually from Quebec "allowing the province to reduce its use of natural gas to generate power." The province further boasted the shift from Ontario-produced natural gas power to Quebec-produced water power will be good for the environment, cutting annual greenhouse gas emissions by about one million tonnes. Well, it also cut jobs, at home. Fast forward to January, and you will note that natural gas 'non-utility generators' (NUGS) throughout Ontario are starting to shut down, exactly as we forecast would happen. In my home town of North Bay, the NUG here has been idled, and 11 people were sent home. The same can be said for another half-dozen plants across Ontario – putting some 85 people out of work.

February – Taking a closer look at the numbers

A couple of long-overdue reports from the Province of Ontario were finally released. Under the *Fiscal Transparency and Accountability Act*, the Ministry of Finance has several legal obligations to meet, with respect to financial disclosure. This government has not met those obligations. One of these demands that "Within two years after each provincial election, the minister shall release a long-range assessment of Ontario's fiscal environment." Another chapter of the Act requires the Minister of Finance to release the province's 3rd Quarter Finances annually, by the 15th of February.

In October 2013, two years after the 2011 election, the government did not produce the document. Six months later, after repeated requests from my office, they finally released the report. Fast forward to June 2016, two years after the 2014 election, and again ... no report. I made repeated requests to the minister and finally, eight months late, the government produced the *Ontario Long-Term Report on the Economy*.

The report confirmed what experts have been saying all along – Ontario's long-term economic prosperity has been critically damaged. It paints a picture of slow growth and an economy that will continue to shift from good-paying manufacturing jobs to more part-time and temporary employment. In the first six pages, the report stated "Growth in services continuing to outpace the trade in goods"; "The structure of the Ontario economy will continue to shift from goods-producing to service-producing sectors"; and "Shifting employment from goods-producing industries, in particular manufacturing, to service sector industries." The report also projects a drop in the growth of Ontario's GDP, a decline in private sector savings, imports, exports, labour participation rate, in fact nearly all of the major economic indicators.

However, here are some of the facts the report fails to address:

- Foreign direct investment in Ontario dropped this past year, from $7 billion to $4 billion. Ontario's market share has been cut in half from 12% in 2015 to just 6% this year – *The ƒDi Annual Report 2016*

- Private investment to decline 0.7% in 2016, with an 8% drop projected for manufacturing sector – *Financial Accountability Office's Ontario Business Investment Expected to Edge Lower in 2016*

- Business investment in the province declined by 0.8%, including a drop of nearly 6% in investments in machinery and equipment – *Ontario's Economic Accounts for the 3rd quarter of 2016*

- $2.74 billion in revenue from service fees in 2016-17, a 38.7% increase from 2011-12 – *Financial Accountability Office*

- Deterioration in the province's budget balance, with a deficit of $1.7 billion by 2020 and Ontario's net debt projected to rise over the next five years to a record total of $350 billion – *Financial Accountability Office*

- Ontario currently has the highest debt burden among the major provinces, carrying $2.40 in net debt for each dollar of provincial revenue – *Financial Accountability Office*

- Interest payments on debt will total nearly $11.8 billion this fiscal year – *Minister of Finance's Quarterly Financial Statement*

More missed deadlines

Despite the legal requirement, the government again failed to provide the *2016-17 3rd Quarter Finances* by the February 15 deadline. While they did deliver a report six days later, this is the first time they have produced a report in eight years, repeatedly withholding important financial information from the media, opposition, and taxpayers. Ontario's Financial Accountability Office (FAO) has warned of the government's "broader pattern" of secrecy and their refusal to provide information was making it "difficult to assess the plausibility of the government's financial projections and to evaluate risks that those projections would not be met."

The report states that contrary to the information provided by the FAO, the government shows they will balance the budget next year. Closer inspection of the revenue sources reveals $600 million from reserves, $500 million more in unplanned revenue from the Land Transfer Tax, additional revenue from service fees, and the sale of one-time assets such as Hydro One. In addition, and contrary to the ruling from the Auditor General, the government is including the surplus pension funds. (More on that later).

The Chamber weighs in

The third report came from the Ontario Chamber of Commerce. For five years their annual analysis was titled *Emerging Stronger.* This year, as an acknowledgement that the name was purely aspirational, the Chamber chose *Ontario Economic Report 2017*, to be more accurate. The most stunning revelation was that only 24% of businesses have confidence in the province's economy. Since the Premier first took office in 2013, business confidence in the provincial economy has been cut in half, from 48%. Interestingly, despite a lack of provincial confidence, 62% of members are confident about their own organization's economic outlook.

In addition to the Business Confidence Survey, the report also contains the Business Prosperity Index, and the Economic Outlook, providing a snapshot of the year that was and the year ahead. It's a must-read report found at OCC.ca

Ignoring the Auditor General

The government continues to ignore the ruling of the Auditor General. Recall that AG Bonnie Lysyk concluded that pension plan surpluses shouldn't be included on the province's balance sheets as an asset, because the government can't access them. The government then budgeted $435,000 to empanel a committee to review the AG's decision. This private panel concluded that the pension surpluses should be counted as assets. The government has stated they will implement the panel's advice and will use it in preparing the province's financial statements.

AG Bonnie Lysyk says she won't give her "seal of approval". She's insisting on seeing letters from the Ontario Teachers' Federation and OPSEU, showing a formal negotiated agreement with the government, stating they can use that money. The government says that joint pension agreements already spell out how surpluses are handled, so no letter is needed.

Minister calls MaRS building debacle "Fake News"

The MaRS building real estate bailout has resurfaced after three years. First and foremost, the work the men and women perform within the MaRS building is exceptional, ground-breaking, and very exciting. And the companies located there are world-class. But the 2014 scandal had nothing to do with the tenants and their employees. It was about the government providing a secret $308 million bailout to a U.S. real estate firm – until a whistle-blower slipped a brown envelope under our door.

When the bailout hit the media, it was a top story for several days, with comparisons being made to the e-Health and gas plant scandals. The real issue was, once again, the government was not being open and transparent. Instead of coming clean and letting the public know the building's owner was in trouble because only one-third of the building was leased out, the government secretly bailed the firm out. They had the taxpayer assume the risk and tied up hundreds-of-millions of dollars for years. The Auditor General called it "a high-risk bailout".

Early in February, when three financial services firms announced their investments in MaRS will be used to repay the money, the government didn't hide that from the public. They held a news conference where the Minister of Economic Development and Growth called the 2014 headlines of the bailout "fake news". So, if you're caught red-handed because of a whistle-blower, and the AG calls what you did "a high-risk bailout" – when the issue is resolved three years later, somehow the original debacle was "fake news"? The Minister later took to Twitter to apologize for his comment.

The story should have ended there. Instead, the Minister doled out some fake news of his own. In his speech and media scrum, he talked about Ontario's economic growth, foreign direct investment, and employment growth.

The Minister stated that Ontario's economy is growing faster than the U.S. That's not at all accurate, as last year's numbers show that Arkansas, Washington, and Oregon all had higher annualized growth of 3.9%, while Colorado matched Ontario.

He also stated that Ontario is the top foreign direct investment destination. That's not true. As I mentioned earlier, investment dropped from $7 billion to $4 billion, and Ontario is no longer the top destination; we have fallen to 4th place, behind California, New York, and Texas.

In a Letter to the Editor, in a speech to the Legislature, and again at the news conference, the Minister stated our employment is "the best in Canada" and "We're leading the country in job creation". Again, the facts are quite different. Our unemployment rate is higher than B.C., Manitoba, and Quebec, and tied with Saskatchewan. And internal Ministry of Finance documents revealed "there are fewer jobs today relative to the population … employment growth has not kept up with the growth of the working-age population".

Between stories like these and the "broader pattern" of secrecy, you can understand the FAO saying it is "difficult to assess the plausibility of the government's financial projections".

March – Hydro Hail Mary

With the government slumping in the polls due to skyrocketing hydro rates (almost 400% increase in 14 years), and with families being forced to decide whether to heat or eat, the government launched their so-called *Fair Hydro Plan* at the beginning of the month.

The media headlines describe the sentiment regarding the hydro plan best … "Sleazy, desperate hydro ploy to fool Ontarians"; "Cutting today's hydro bill, for today's votes, with tomorrow's money"; "Hydro slash will cost us"; "Hail Mary"; "$25B hydro boondoggle"; and "Hydro on Layaway".

Why is the government doing this?

This is probably the most interesting part of the story. I revealed this in last year's *Focus* book. To re-cap, government pollster David Herle gave a presentation to an energy association. His first slide read "Rates are an increasingly major concern in Ontario. The cost of electricity is not just seen to be unreasonably high; it is widely seen as damaging to the provincial economy." He told the government that people like the elimination of coal, improved reliability, conservation, and renewable energy. Now, you certainly don't want to blame the cost hikes on things people like, even if that's actually why costs are skyrocketing. Instead, the blame could be focused on several hot-button issues, such as the billions spent on upgrading transmission lines, because surveys show reliability is important (even though the transmission lines they built actually were to bring power from far-flung wind turbine locations, not to "upgrade an aging system" as they claimed). Again, none of the talking points need to be based on facts – where's the fun in that?

In the Premier's Toronto Star column, she wrote "Brownouts, blackouts, and dirty coal endangered our economy. We closed all of Ontario's coal plants, built thousands of kilometres of new transmission lines, and introduced renewable energy. Ontario now has a clean, reliable system with a modern, diverse mix of generating sources. But – all this came at a price. We put the $50-billion cost of the rebuild onto the hydro bills of just one generation."

Sadly, her words are just that – words. There are no facts behind them. Think they've built a reliable system? *Blackout Tracker Annual Report* revealed the number of Ontario outages increased by 275% from just 2012 to 2015. And in the Auditor General's 2015 Annual Report she revealed, "Most of the increase in what consumers pay for electricity has come from generation cost increases, which account for 60% of the overall cost of electricity. Generation costs have increased by 74% over the last decade." Despite the government's talking points, we know that signing contracts for power we don't need, is what caused (and continues to cause) electricity bills to skyrocket.

What is the government doing?

The Ministry's slide deck shows the plan has four major components: refinance the Global Adjustment (GA); enhance consumer rebates; lower the Industrial Conservation Initiative threshold; and find efficiencies in the market.

The GA bucket is where most of the sins lie, as it's the difference between market price and what the government pays for power, plus all other hydro-related costs. The Auditor General told us "GA fees have increased significantly, from $650 million in 2006 to $7.03 billion in 2014." She added "Electricity consumers have already paid a total of $37 billion, and they are expected to pay another $133 billion in GA from 2015 to 2031." The government's number used in the announcement put the 2017 GA over $12 billion. The refinancing plan would spread the costs over a longer period of time, by reducing about $2.5 billion per year over 10 years, for an additional accumulated debt of about $28 billion.

The enhanced consumer rebates consist of broadening the Rural or Remote Electricity Rate Protection ($500 million in the coming year; funded by provincial revenues); enhancing the Ontario Electricity Support Program ($185 million in the coming year; funded by provincial revenues); First Nations On-Reserve Delivery Credit ($20 million in the coming year; funded by provincial revenues); and establishing a New Affordability Fund ($200 million in the coming year; funded by provincial revenues). The total cost to the tax base is $905 million annually. This is on top of the roughly $1 billion required from the tax base to pay for the 8% HST rebate.

The Industrial Conservation Initiative will target industries with the NAICS codes 31-33 and expand the eligibility to manufacturers with average monthly peak demand over 500KW. The cost to the ratepayers is yet to be calculated.

The last area is finding efficiencies or as the government says, 'bending the cost curve'. The government feels that the changes they will make to future initiatives are estimated to save at least $200 million per year, starting in 2021.

One interesting side-note is that the government has co-opted OPG into their scheme. The slide deck states that OPG "Finances/manages the GA proposal". Why, you might ask? Well OPG is certainly large enough to absorb this massive financial hit, but primarily … they are two steps removed from the province … and this liability doesn't show up on the province's books. Burying this purported fix inside of OPG's balance sheet does nothing to solve the government's bad contracts crisis. Instead, it simply masks the consequences of this Hail Mary. It's inappropriate and risky for OPG.

As you can see, there is nothing here that fixes any of the hydro problems. The government will continue to sign contracts for power we don't need and continue with escalating hydro rates from the further sale of Hydro One. This is simply financial engineering – no solutions; just accounting changes. All in, it's expected this will add about $50 million in financing costs to both the ratepayer and the taxpayer. (In the May chapter, the Financial Accountability Office reveals their analysis. I wasn't too far off!).

And now take a bow

The government was so eager to spread the word about their plan, that rather than tabling it in the Legislature, having a debate, and voting on it, they just went ahead and bought $1 million worth of taxpayer-paid advertising. And they tell us there's more to come. The Auditor General weighed in calling the ads a "pat-on-the-back" and could be considered partisan. She also said the ads likely wouldn't have been approved under old government advertising rules. But remember … the government changed the advertising rules to allow partisan ads to run, and the AG's approval has been reduced to a rubber stamp. The Auditor was so incensed by the changes that she penned a Special Report to the Legislature decrying the changes. She said changing the rules would end up giving taxpayers the bill for millions of dollars of partisan ads. "Sure enough, the government walked right through that open door," she added.

What did $50 billion get us?

Recall the Premier stated the government spent $50 billion on the cost of the rebuild. But her own Energy Minister issued a news release claiming Ontario had "invested more than $35 billion" in new and refurbished generation. So, between them, their talking points differed. My retired banker friend and frequent National Post energy columnist Parker Gallant beat me to the punch and has created a comprehensive list. His findings are here:

Frills and shiny baubles:

Smart Meters	$2.0B
Smart grid	1.2B
Coal plant write-off	.6B
Conservation	2.5B
Cancelling gas plants	1.1B
	$7.4B

Unreliable & intermittent power:

Wind generation	$10.2B
Solar generation	5.2B
Transmission connections for above	5.0B
	$20.4B

Photo-op generation:

Beck hydro tunnel ($600M over budget)	$1.5B
Mattagami hydro project ($1B over budget)	2.6B
	$4.1B

Value for money:

Bruce Nuclear refurbishment	$3.4B
	$3.4B

This is indeed shy of the $50 billion the Premier says was spent, but the number lines up with the Energy Minister's claim. Nonetheless, this proves that the bulk of the money did not go towards "the cost of the rebuild." It went to intermittent and unreliable wind and solar projects (like the AG said it did), which are unable to deliver generation when the wind isn't blowing and the sun's not shining. The second largest category created no generation, nor improved transmission, nor reduced blackouts or brownouts.

We now understand why the government did this. Their polling numbers were terrible, and people saw the hydro crisis as damaging to the economy. The pollsters convinced them the solution was to tell people what they needed to hear. We also now understand what they did. It was purely financial engineering – nothing whatsoever to do with fixing the systemic problems with hydro. And they co-opted OPG into being their bank for the financing of their scheme. Then they used taxpayer's money and changed the rules to allow partisan advertising to tell the people of Ontario how good this plan was, before even tabling it in the Legislature.

April – 2017 Budget: Pay more; get less

The 2017 Budget is more proof that Ontario families will continue to pay more and get less.

While the government has announced that they have 'balanced' the budget, this is far from reality. Readers of my *Focus* series have known for months, if not years, that there would be no balance. The once-confidential Gas Plant Scandal documents were very clear, in the Ministry's own words – "the government is not on a path to balance." And that was before the deficits took a further move south under our current Premier. Then all of a sudden, the province's fortunes shifted, to the tune of billions of dollars. But before you look for any kind of spending controls to make that shift, look again at the 'special' revenue.

The government started adding 'Asset Optimization' funds each year – billions of dollars worth. In 2014 it was $1.1 billion, which included the sale of their GM stock – straight into revenue. In 2015, another $1 billion – all from one-time asset sales; straight into revenue. 2016 was a banner year, where they booked an additional $2.2 billion over the 2015 forecast. The budget states this was "...due to higher revenue from asset optimization in 2015-16" which consisted primarily of revenue from the sale of Hydro One shares. They also received $800 million more in land and sales taxes "due to Ontario's strong housing market."

In this budget, they have "overachieved" as the Finance Minister so frequently tells us. Only, a significant amount of the revenue bump is from one-time sources. It starts with a $1.5 billion increase in infrastructure revenue from the Feds. This is traditionally a $100 million fund, but the Feds are investing in infrastructure, so this is a temporary bump. Land Transfer Tax is also up a further $400 million this year (it was up $600 million last year). One-time asset sales are up $1 billion. New this year we see $1.8 billion in cap-and-trade tax added straight to revenue. And finally, $500 million is booked from the Teachers' Pension Plan, even though the Auditor General said she would not allow it.

Add up the real one-time funds, and there is a $5 billion hole in the budget. We have a structural deficit. We spend more money every year, than we take in. The Financial Accountability Office repeatedly bares this out.

You will hear the government say that the funds from the sale of Hydro One and from cap-and-trade will go into the Trillium Trust and be used for infrastructure. On the surface, they're correct. But they slipped ONE sentence into each of those Bills to give themselves an out. Bill 144, which facilitates the sale of Hydro One, has a great line in Schedule 22, Section 7, Paragraph 2, which states ..."to <u>reimburse</u> the Crown for the expenditures incurred to fund costs relating to infrastructure." This Ottawa Citizen quote sums up what is really going on.

> A reasonable person might wonder why we need to sell most of a significant public asset, just to keep doing what we have been doing for years. The real answer, I suspect, is that putting some billions of new money into the province's transit trust will enable the government to quietly shift existing money to help it reduce the deficit or pay for other spending".

And that is indeed what Schedule 22 allowed the government to do – put the sale money into infrastructure, and take the money already budgeted for that infrastructure and apply it against the deficit.

It worked so well for the sale of Hydro One, the government did it again with the revenue from cap-and-trade. As mentioned earlier, Bill 172, which facilitates the cap-and-trade deal, does this in Schedule 68, Section 2, Item 3, which states ... "to reimburse the Crown for expenditures incurred for transportation, public transit vehicles, and infrastructure." Again, they put the revenue into infrastructure, and take the money already budgeted for that infrastructure and apply it against the deficit. There you have it – an easy way to tell the people one thing, when the real intent is completely different.

The Finance Minister also announced that not only are they balancing this year, but next year, and the year after that one too! I mention this because the budget book only forecasts to 2017-18. There are NO numbers beyond that. Even last year's budget went out to 2018-19, which means this year's budget is missing 2 years of forecasts normally included.

The reasons become more evident as you read deeper into the budget. Ontario's economic growth is forecast to fall from 2.7% to 2.3% this year and down to 1.7% in 2020. Our employment growth will fall to 0.9% in 2020. Job creation will tumble from 94,000 jobs next year to 66,000 in 2020. And housing construction starts are scheduled to slide from 75,000 in 2016 down to 68,500 in 2018. All these affect revenues – so it's best just to ignore putting any future revenue numbers in the book! The book itself is about 70 pages shorter than previous versions and is chock full of colour photos. It appears to be more of an election-positioning budget rather than a financial document.

By the numbers

- Total program spending is up $6 billion, to a record $141 billion.
- Interest on the debt rose, from $11.2 billion to $11.6 billion.
- Debt has increased from $302 billion in 2016-17 to $312 billion in 2017-18. It is projected to increase to $323 billion by 2018-19 and $336 billion by 2019-20. Incidentally, debt was $139 billion when this government took over in 2003.

Why does balancing matter?

The Auditor General devoted considerable space in her 2014 and 2015 Annual Reports to discussing Ontario's growing debt burden. This debt has significant implications in your day-to-day life. Specifically, Auditor Bonnie Lysyk wrote "The negative impacts of a large debt burden include debt-servicing costs that divert funding from other programs." This is why we're seeing 1,600 nurses fired in Ontario. My own local hospital in North Bay has seen 388 frontline healthcare workers fired in the last five years – and that includes 100 nurses. This is exactly what the Auditor was referring to – and exactly why you should care whether the government runs a balanced budget or not.

In her 2015 Report, the AG instructs the government to provide "long-term targets for addressing the current and projected debt" and to "develop a long-term debt-reduction plan outlining how it will achieve its own target of reducing net debt to GDP from its current 39.5% to the (Premier Harris era) ratio of 27%." As mentioned above, Ontario's debt has ballooned to $312 billion – up from the $285 billion it stood when the Auditor gave her last warning.

What's not in the budget

What you won't see accounted for is the 25% reduction of hydro bills. Under the so-called Fair Hydro Plan, there are four major components: refinance the Global Adjustment (GA), adding an additional accumulated debt of about $28 billion; enhance consumer rebates, at a cost of $905 million, plus the $1 billion required from the tax base to pay for the 8% HST rebate; lower the Industrial Conservation Initiative threshold, with the cost to the ratepayers yet to be calculated; and find efficiencies in the market, to save at least $200 million per year, starting in 2021. As outlined earlier, the government has co-opted OPG into their scheme, so these liabilities don't show up on the province's books. This is inappropriate and risky for OPG.

May – Hydro plan … not so fair

The Financial Accountability Office (FAO) released *An Assessment of the Fiscal Impact of the Province's Fair Hydro Plan* (FHP). The FAO estimates that the proposed FHP, consisting of the provincial HST rebate, electricity cost refinancing, and changes to electricity relief programs, will cost the province $45 billion over 29 years (Remember my estimate of $50 million, two months earlier), while providing overall savings to eligible electricity ratepayers of $24 billion. This results in a net cost to Ontarians of $21 billion.

However, the estimated $45 billion cost to the province assumes that the province is able to achieve and maintain a balanced budget over the next 29 years. In the *FAO's Fall 2016 Economic and Fiscal Outlook*, and again in the *Spring 2017 Economic and Fiscal Outlook*, they project continued budget deficits over the same period. If the province is unable to balance the budget and borrows to fund the hydro scheme, the FAO says the cost to the province could increase to between $69 billion and $93 billion.

The FAO also adds another twist; one which I first introduced to the Legislature earlier in the year. When the government launched the FHP, they coopted Ontario Power Generation (OPG) into their scheme. They announced that OPG would be managing and financing the proposal. Why, you might ask? Well OPG is certainly large enough to absorb this massive financial hit, but primarily … they are two steps removed from the province … so this liability won't show up on the province's books.

Acknowledging that, the FAO stated "The electricity cost refinancing initiative involves a complicated accounting structure that will increase gross debt by approximately $26 billion by 2027- 28 but does not impact the province's net debt due to the creation of a regulatory/investment asset; essentially an obligation for ratepayers to repay the province approximately $26 billion." Due to the nature of the proposed financing transaction, (involving OPG) the FAO recommends that Members of Provincial Parliament obtain assurance from the Auditor General that the province's proposed accounting treatment for the electricity cost refinancing meets public sector accounting standards and will not impact the province's annual surplus/deficit and net debt."

That same day, the Auditor General appeared at the Standing Committee on Justice Policy; the Committee studying the government's hydro scheme. She stated right out of the gate that she wanted to make sure the 25% hydro rebate was "properly recorded in the consolidated financial statements of the province and is transparently reported." She then laid bare that "the government plans to borrow about $26 billion … but it does not want to reflect the overall impact of these borrowings on the consolidated financial statements." She acknowledged, as did the FAO, that the government planned to "record anticipated revenue as an asset to offset borrowings." "As a result, (of attempting to use OPG) there will be no impact on the net debt." She then repeated, three different times, "this is NOT allowed under Canadian public-sector accounting standards."

Despite the government's efforts to keep that additional debt off their books, the AG insists it be reported properly. In addition, the accounting dispute isn't just about the numbers in question; it also puts the government's integrity in question. If the additional data from the Financial Accountability Officer and the Auditor General are acknowledged, then that would be the true state of Ontario's finances.

June – Sifting through the numbers

The Financial Accountability Office (FAO) released a further report; their *Spring 2017 Economic and Fiscal Outlook*.

The first sentence of his release says it all. "Based on our analysis, the FAO is projecting continued Ontario budget deficits over the next five years."

The report provides the FAO's current economic forecast and an assessment of the province's fiscal outlook. It incorporates information from the 2017 Ontario Budget, Ontario's Economic Accounts, Statistics Canada, and internal FAO resources.

The FAO added that because of a one-time boost in non-tax revenue, for the current fiscal year they project an improvement in the deficit. "But beginning next year, the FAO projects a steady deterioration in Ontario's budget deficits due to moderating revenue growth combined with higher expenses."

The economic outlook

The FAO's economic outlook provides the foundation for their fiscal projections. Ontario saw its real GDP growing 2.7% in 2016. For 2017, the FAO forecasts real GDP to rise by 2.4%. They also, like the consensus outlook of private economists, anticipate growth will moderate slightly over the next four years, with average annual gains of 2%.

But they address the risks to this economic forecast, primarily the uncertainties of the policy direction of the U.S. They feel "This uncertainty could deter Ontario business investment, hurting the province's economic prospects." In addition, they feel that Ontario's surging housing market continues to be a major concern. In 2016, investment in residential housing accounted for a record high of 8.3% of Ontario's nominal GDP. In 1989 it soared to 8.2%, only to tumble to 4% by 1996. The FAO concluded "A sharp correction in housing prices could reverberate beyond the housing market and lead to broader, economy-wide impacts."

The fiscal outlook

For 2017-18, the government has committed to balancing the budget. But the FAO says the budget will benefit from "a $3 billion boost in onetime non-tax revenues this year." They describe these as "temporary revenues" and they include "an increase in federal transfers for infrastructure, additional sales of public assets, including the recent sale of Hydro One, and additional one-time cap-and-trade proceeds." They warn "However, beginning next year, the growth in tax revenues is projected to be moderate, while the boost from one-time non-tax revenues will end."

On the expense side, the FAO projects spending growth of 3.3% per year, over the outlook. This is based on the government's 2017 Budget, and includes significant new spending across all sectors, including the new drug program, child care spaces, increased funding for hospitals, and the government's so-called 'Fair Hydro Plan' (FHP) 25% hydro rebate.

While combining the revenue and expense projections should normally provide all one would require to develop an outlook, there is a twist here in Ontario. The FAO provided two varying projections, to account for the ongoing battle between the government and the Auditor General (AG) on the application of government accounting standards for two jointly-sponsored pension plans. The FAO felt compelled to present the two different accounting treatments to have people better understand the implications of the different accounting interpretations.

Based on the AG's treatment for the pension assets, the FAO projects significant budget deficits over the entire outlook. "On this basis, it is unlikely that the government will balance the budget without significant fiscal policy adjustments to raise revenue or lower expense." Under the government's accounting, the FAO projects that a balanced budget is within reach in 2017-18 "in part because of the significant one-time revenues described earlier." They continued with "Beyond 2017-18, the deficit is projected to deteriorate steadily due to rising expenses and slower revenue growth."

Debt

Again, there are two tracks to take here; one based on the Auditor General and another based on the government's numbers. Under the AG's treatment, the FAO projects Ontario's debt to grow by $76 billion over the next five years, reaching $390 billion. That would put the net debt-to-GDP ratio at 40.3% by 2021-22. Under the government's accounting, the FAO projects Ontario's net debt will increase by $62 billion to $365 billion. This would edge the net debt-to-GDP down to 37.5%. Given their analysis of rising deficits, combined with the government's planned infrastructure investments, the FAO concludes "achieving these debt targets will likely require significant additional fiscal measures under either accounting presentation."

When the FAO presented this outlook, I asked if data from the government's hydro scheme (last chapter) was included. The answer was no, as their report on hydro had only been released days before. I bring this up as there were significant revelations in that report which will affect Ontario's debt.

July – Financial house of cards

Two separate issues arose that either reflected or affected the state of Ontario's finances. The first featured a large and varied group of analysts who independently outlined the true state of Ontario's economy, and the reasons behind it. The second was Hydro One's announcement of their planned purchase of U.S. utility Avista.

Economic recovery?

Each quarter, the Conference Board of Canada publishes their *Provincial Outlook Economic Forecast,* providing their short-term outlook for Canada's provinces. While they forecast a number of provinces will perform better in 2017, Ontario and B.C., which led the provinces in growth for 2016, will see slower economic growth. This was backed up by several other analyses published over the month.

Phillip Cross authored *Ontario's One Cylinder Economy*, focusing on housing in Toronto and Ontario's weak business investment. He illustrated the province's increasing dependence on Toronto's housing market for growth, leaving it especially vulnerable if the market slows. The Financial Accountability Office outlined the same concern in their *Spring Economic and Fiscal Outlook*. They stated "The relative importance of residential housing investment to the overall economy has increased substantially in recent years, posing a significant risk to the Ontario economy, in the event of a sharp housing market correction." The FAO also pointed out that residential housing accounted for a record 8.3% of Ontario's nominal GDP and that back in 1989 it hit 8.2% before tumbling to just over 5% in 1991 and falling to less than 4% by 1996.

Cross' paper also identified several factors that are currently at play in Ontario, discouraging business investment. Ontario has amongst the highest all-in electricity costs in all of North America. According to the Auditor General, provincial government policy decisions increased hydro costs by $37 billion between 2006-14. Outside of Atlantic Canada, Ontario has the highest labour costs, and minimum wage is poised to increase to $14/hr January 2018, and $15/hr by 2019. And in addition to many regulatory burdens, Ontario has the 2nd highest marginal personal tax rate in North America, at 53.5%. As a result of the high cost of doing business, manufacturing sales are little changed since 2003, compared with gains of 14% in Quebec and more than 20% in B.C. and Alberta. Manufacturing investment has been halved since before the recession in industries such as computers and electronics, lumber, paper, printing, rubber, and plastics. Overall business investment has actually fallen from $53.8 billion in 2008 down to $50.9 billion this year.

The Canadian Federation of Independent Business' *Business Barometer Index* showed Ontario took a nosedive, dropping 10 points to 58, the largest month-to-month drop in its history. They claim the tumble is policy-based, referring to sweeping labour standards legislation, which appears to be adding considerable uncertainty over future operating conditions in Ontario.

CFIB Survey Results (more than 3,500 member responses)	
Which of the following actions would your business take as a result of (the proposed) minimum wage increases?	
Increase prices	66%
Reduce hiring	64%
Less employee hours	53%
Cut employees	43%
Consider closing, or moving out of Ontario	34%

According to fDi Intelligence, Ontario is now the #3 destination for foreign direct investment, with $4.5 billion. They inched ahead of Texas, which slipped from 2nd to 4th place, at $4.4 billion. In both 2014 and 2015, Ontario was ranked #1, receiving U.S. $7.1 billion in foreign capital.

S&P Global raised Quebec's credit rating from A+ to AA-, meaning that for the first time ever, Quebec's credit rating ranks higher than Ontario's. The agency stated that over the next couple of years it expects Quebec to keep its budget in the black and its debt ratios in decline thanks to strict cost controls, growing tax revenues, and prudent fiscal policies. This has boosted the confidence of businesses considering Quebec as a destination for investment. At the same time, S&P lowered Ontario's short-term rating to A1 from A1+, leading to the concern that business will have to shoulder any increased costs, adding a further chill to the Ontario investment climate.

Finally, the Fraser Institute's Ben Eisen weighed in with various commentaries on Ontario's 'recovery'. "From 2003-14, inflation-adjusted economic growth per person in Ontario averaged 0.3% annually – a third of the national average. From 2004-14, annual private-sector job growth in Ontario averaged 0.6% – approximately half the rate of job creation in the rest of Canada. As a result, average incomes in Ontario fell relative to the rest of the country. In 2012, average disposable household income in Ontario fell below the national average for the first time." His releases prompted back-and-forth letters between the Finance Minister and Eisen – and I couldn't help but weigh-in with my own Letter to the Editor, which was published, outlining further supporting facts about the real state of Ontario's economy.

The Hydro One/Avista deal

Hydro One announced a deal to acquire Avista Corporation for $6.7 billion, in an all-cash transaction. The deal is expected to close in the second half of 2018, and is still subject to approval from common shareholders and various regulators. Avista shareholders will receive US$53 in cash per common share; a 24% premium over the market close on the day of the announcement. Moody's and S&P reacted swiftly by changing Hydro One Inc.'s credit outlook from stable to negative. Recall that following the sale of Hydro One shares, their credit rating was downgraded twice in two months, from A1 to its current A3. Avista provides natural gas and electric service to about 350,000 homes and businesses across Washington, Idaho, Oregon, and Alaska. Hydro One services 1.3 million customers.

The deal is not without several controversies. It puts Ontario back in the "dirty coal" business, as the government so fondly described the industry in the past. Avista owns a 15% stake in two units of the Colstrip coal plant in Montana; the second-largest coal-fired plant west of the Mississippi. It is one of the U.S.'s top 20 greenhouse gas-producing plants and responsible for an 800-acre coal ash waste pond. In addition to the optics of supporting "dirty coal", there's the reality of the estimated $1 billion clean-up of the pond. Avista's share could top $100 million, and the concern is that Hydro One ratepayers may be on the hook. This took on a new level of concern when Avista CEO Scott Morris stated the sale means "we can spread out costs over a larger customer base."

Hydro news keeps coming

The Ontario Society of Professional Engineers (OSPE) reported that in 2016, the province wasted a total of 7.6 terawatt-hours of clean energy – an amount equal to powering more than 760,000 homes for a year, or $1 billion. That's a 58% increase over the amount wasted in 2015. All this happening "while the province continues to export more than 2 million homes-worth of electricity to neighbouring jurisdictions for a price less than what it cost to produce," said Paul Acchione, former President and Chair of OSPE.

The $1 billion loss happens when power is not needed in Ontario, and could not be exported, so it is simply dumped. "It's when we tell our dams to let water spill over top, our nuclear generators to release their steam, and our wind turbines not to turn, even when it's windy," said Acchione. In addition, power was exported from 2014-16 at prices much lower than the total cost of production because Ontario produces far more electricity than it can use, so it is forced to sell this surplus power at a loss. "Taken together, those represent nearly enough electricity to power every home in Ontario for an entire year," said Acchione.

This was followed up with a shocking report from the Fraser Institute, *Evaluating Electricity Price Growth in Ontario*, revealing that Ontario has the fastest-rising hydro prices in the country – and poor policy is to blame. As for the so-called Fair Hydro Plan, which went into effect in July, the "government has just covered up serious problems in the system by shifting the cost onto taxpayers and future hydro bills," stated co-author Kenneth Green. "What hasn't changed are the government-driven decisions to favour costly wind and solar power purchased at above-market prices," he added.

"These political decisions are the reason Ontario electricity prices soared by 71% between 2008-17, while the average growth across the country was 34%," said Green. Last year alone, Ontario realized a 15% increase in prices, over the previous year. As a result, July also saw several Ontario facilities either close or move due to skyrocketing hydro rates. Paul From, President of Central Wire Industries, announced their plant in Erin will cease operations, sending 26 workers home. He directly attributed the decision to the high cost of electricity.

July offered a harsh reality, with so many groups weighing-in on the true state of Ontario's economy and finances. From concerns over the dependence on Toronto's housing market, the factors creating a discouraging business climate, falling foreign capital investments, and the anemic private-sector job growth, there is certainly evidence that Ontario cannot continue in its current direction.

August – Ontario's financial hole

In what appears to be a repeat of last month's financial summary, this month saw another large and varied group of analysts independently present what they feel is the true state of Ontario's economy, in response to government releases. And again this month, the hydro file played a role.

Deeper in debt

The month began with what the Toronto Star's QP Briefing called "a blistering Fraser Institute report." Its title, *Wishful Thinking: An Analysis of Ontario's Timeline for Shrinking Its Debt Burden*, suggests there is no realistic plan to get out of their financial hole. The report details how the government's timeline for reducing the province's historically high debt burden relies on optimistic and questionable assumptions and lacks a detailed, credible plan to achieve it.

The government has acknowledged that at 37.5%, the province's debt-to-GDP ratio is too high. (It fell just 1.6% in the last three years.) When the current government took office in 2003 it was 27% – a number it is targeting to return to by 2029/30. Unfortunately, the government has offered no specifics on how it will get back down to that number. "Queen's Park has picked a target date for reducing its debt burden several years from now and is simply hoping, somehow, that the mountain of debt it created will start shrinking on its own," said Ben Eisen, co-author of the report.

The debt ratio reduction will have to nearly triple its current pace to meet the target, and essentially no new debt could be added after 2021. Rather than a pro-active plan to restrain the growth in debt, the government is relying solely on improved economic growth for the next 12 years, and assumes no economic slowdown or recession.

Stephen LeClair, Ontario's Financial Accountability Officer (FAO), backed up the Fraser report charging that the government's plan to lower its net debt-to-GDP ratio is overly optimistic. He says the government will have to get creative if it wants to hit its debt reduction targets, adding it will take some fiscal policy maneuvering. "It's going to be challenging for the government to achieve its debt target without significant additional measures to raise revenue or lower expenses," he told QP Briefing. "They don't say in the budget as to how they will achieve it," added LeClair.

Ontario's Finance Minister rebutted the report in a Letter to the Editor (to which I responded with my own LTE). That prompted Ben Eisen to respond with a media column of his own, entitled *Debt, Part 2*. He highlights how in its recent history "Ontario has suffered from economic stagnation and relative decline compared to the rest of Canada." He also revealed that between 2003 and 2015 "Ontario's inflation-adjusted per-person GDP increased at an average annual rate of just 0.4%; less than half the growth rate in the rest of Canada." In fact, in 2012 "real disposable household income in Ontario slipped below the Canadian average for the first time in recorded history."

Eisen ended his column with sage words for the government. "You can't have it both ways; blaming forces outside government control for periods of economic weakness, while crediting prudent government decisions for good economic news." Again, I couldn't help but offer my own Letter to the Editor, which was published.

Letter to the Editor:

> *It was troubling to read Finance Minister Charles Sousa's rebuttal ("Ontario's doing fine," Aug. 8) to Ben Eisen's column on Ontario's debt. Eisen delivered a blistering revelation of Ontario's debt burden and the snail's pace at which it is being addressed. It reminded me of the Auditor General's dire warnings in consecutive Annual Reports, where she said "Ontario's debt continues to grow faster than the province's economy." She warned the consequences of this higher debt would result in "the crowding out of other spending," which is happening right now in areas such a frontline health care. Eisen further reports the province is using "questionable assumptions" and "wishful thinking" as part of its*

debt reduction plan. The Financial Accountability Office (FAO) agreed, suggesting the (government) plan is too lofty.

Meanwhile, Charles Sousa would have us believe that everything is just fine. He wondered why Eisen failed to mention his balanced budget, and quoted a debt-to-GDP number of 37.8%, continuing on a downward track. He also talked about spurring economic growth at a faster rate than debt. All wonderful aspirations … except none are remotely accurate!

The FAO said a balanced budget is only within reach "because of significant one-time revenues." As for debt-to-GDP, he sees it actually growing to 40.3% by 2021-22. The Budget states growth will see average annual gains of 2%, but net debt will easily surpass 3% annually.

Under the (government) Ontario families will continue to pay more and get less.

Victor Fedeli, MPP Nipissing

Ignoring reality

In mid-August, the government released its quarterly finances … on time. I make a special note of that very rare occurrence, as you will recall earlier I mentioned the fact we went several years without 3rd quarter finances ever being released – a flagrant disregard of the *Fiscal Transparency and Accountability Act*. This prompted the FAO to warn of the government's "broader pattern" of secrecy and their refusal to provide information, making it "difficult to assess the plausibility of the government's financial projections and to evaluate risks that those projections would not be met."

The government report states that they're maintaining balance. Unfortunately, the report completely ignored the concerns raised by the Financial Accountability Office and the Auditor General (AG). The FAO was clear – not only does it expect a deficit this year, but a steady deterioration of deficits in the coming years, without either tax hikes or cuts to services. In addition, this report continues to thumb its nose at the AG, who contests the government's accounting treatment for jointly-sponsored pension plans. If properly accounted for, the province would be in a larger deficit position according to the Legislature's independent finance officers.

In addition, there is no accounting for the financing of the government's so-called Fair Hydro Plan. Recall that this is the deal that lowers hydro ratepayers' monthly bills by 25%. It will save ratepayers a total of $24 billion over the next 10 years, but could cost as much as $93 billion to finance, with borrowed money.

The government has ordered Ontario Power Generation to be their financing arm – ostensibly because any borrowing by OPG would not show up on the government's books. This has prompted AG Bonnie Lysyk to claim this is a "dangerous precedent" by keeping the borrowing off the province's books; a move that "does not meet public sector accounting standards." It will be interesting to see this fall, when the AG presents the Public Accounts, to see how she handles the government's statements. They were presented last year, for the first time in history, without the signature of the AG.

More reality

As if the "blistering Fraser report" and the rebuking of the quarterly finances wasn't enough 'tough love', the Financial Accountability Office issued a Commentary: *Optimistic Revenue Projection Underpins Government's Balanced Budget Plan*. Days before, the FAO's release said it all: "The Commentary will highlight the downside risk in the government's forecast and its consequences on their commitment to balance the budget."

In a repeat of what the FAO has been saying to government, month after month, Stephen LeClair stated, "there appears to be a significant downside risk to the government's forecast. As a result, the FAO expects that staying in balance after 2017-18 will require additional fiscal policy measures – that is, new revenues or lower than projected spending." He also stated that if revenues fail to meet the government's "optimistic" targets, that "renewed deficits" are possible.

In a chapter titled "2017 Budget Forecasts Surprisingly Strong Tax Revenue Growth," the FAO states that "after removing the impact of one-time revenue, the budget forecasts revenue growth of 5.5% per year on average from 2016-17 to 2019-20 – significantly above the historical pace of 3.3% since 2004-05." It goes on to say "The budget's forecast for tax revenue growth also seems very strong when compared to the projection for economic growth. Over the past five years, tax revenues increased at the relatively strong average pace of 4.4%, 0.5 percentage points above the average growth in nominal GDP. Over the next four years, the budget is calling for average tax revenue growth of 5.5%, or 1.2 percentage points above the forecast for average nominal GDP growth." It concludes "If the government maintains the spending plans laid out in the 2017 budget, a large shortfall in future tax revenues relative to the budget projection could lead to renewed deficits."

Minimum wage hike

Several organizations and businesses presented their research on the effect of increasing minimum wage to $14 in January 2018 and to $15 in January 2019. The reason these groups were compelled to have independent assessments done is the fact that the government did not provide any research or have a cost-benefit analysis produced.

The Ontario Chamber of Commerce research, conducted by the Canadian Centre for Economic Analysis, concluded there will be "significant, sudden, and sizable uncertainty for Ontario jobs, economy, and communities." The study revealed the measures will put 185,000 jobs at risk in the first two years, impacting Ontario's most vulnerable workers. Data from the economic impact analysis also showed it to be a $23 billion hit to businesses; to increase the cost of everyday consumer goods and services by $1,300 per household; and to add $500 million to the cost of municipalities.

The CEO of Metro Inc. says the grocery industry is facing "significant pressure" over this plan and could be forced to raise their prices to offset the increased labour costs. Several bank analysts agreed, including TD Securities, commenting that "it is tough to imagine the grocery industry simply accepting lower returns that would flow from a "structural change" of minimum wage increases.

Earlier, groups such as the Canadian Federation of Independent Businesses and the Concerned Manufacturers of Ontario weighed in with their findings, concluding that this "government policy is making it almost impossible to compete globally due to uncompetitive costs placed on us in such a rapid time frame." Restaurants Canada was more specific, with 95% claiming this would hurt the very people it was announced it was helping. They said 98% of their members will raise menu prices; 97% will reduce labour hours; 81% will lay staff off; and 74% will explore labour-saving technology such as self-service touch screens.

The most abrupt comments came from Magna, Ontario's largest auto sector employer, who warned they may leave the province. In a submission to the Committee studying the legislation, Magna says Ontario is at a "tipping point" for business and investment. They added "We find ourselves in the very untenable position of questioning whether we will be able to continue to operate at historic levels in this province." In an interview on BNN, Phillip Cross, Senior Fellow at the Macdonald-Laurier Institute said "It's quite unusual for a large multinational firm like Magna, which has to deal with governments all the time, … to even raise the possibility that they would move."

In math and science classes, we were taught to prove our solutions. But this government time and again refuses to do this on key claims and decisions that have large implications for Ontario. They refuse to acknowledge or answer the detailed criticism of the Financial Accountability Office and Auditor General, or put forward an economic analysis to support its policy changes. It's hard to trust claims that can't be backed up by those in government making them.

September – Unlikely assumptions; Significantly misstated

This month began with back-to-back reports from the Legislature's two finance-related officers. You've heard their reports as 'blistering' and 'scathing' far too often, but that's how the media reported both of these, again.

FAO Commentary

The title of the Financial Accountability Office's Commentary, *Ontario's Debt Reduction Commitment Based on Unlikely Assumptions*, says everything you need to know. The FAO projects Ontario's net debt will increase by $76 billion over the next five years, to approximately $392 billion. This will raise the net debt-to-GDP ratio to 40.3%, as opposed to the government's forecast of 36.3%. This is in very strong contrast to the 27% it was at when this government took office, and the 27% target the government hopes to return to by 2029-30.

Their targets are based on achieving balanced budgets over the next 12 years; future capital spending as outlined in the plan; and strong economic growth. The FAO offers that "if any of these relatively optimistic assumptions fall short, the government's 27% debt-to-GDP would not be achieved." It goes on to suggest that "Achievement of the 27% target is based on unlikely assumptions." This is because for the past 30 years, Ontario has rarely achieved successive balanced budgets; in fact, the FAO projects a steady deterioration in the budget deficit over the next five years. The government plan calls for significant reductions in capital spending, yet the FAO says they will likely increase spending. And the government is relying on nominal GDP growing at an average pace of 4%/year; but nominal growth has averaged 3.6% over the past 15 years, and the FAO says that with slower economic growth forecasted, 4% may prove to be too optimistic. Unlikely assumptions.

Auditor General Report

As with the FAO's release, the title of the Auditor General's report, *Ontario Government Understates Annual Deficit and Net Debt*, paints quite a picture. As opposed to signing off on the Consolidated Financial Statements, for the second year in a row, the AG issued a qualified audit opinion, saying "the statements significantly understated the 2016-17 deficit, as well as the province's net debt."

The Auditor General must review the province's financial statements annually and give an opinion as to whether they fairly and accurately reflect the state of the province's finances. The AG issues a *qualified* opinion when, based on the audit evidence obtained, the statements are *significantly misstated*.

Rather than table the annual Public Accounts of Ontario in the Legislature, the government released them four days before MPPs returned from their summer break. After their release, AG Bonnie Lysyk stated "I have issued a qualified audit opinion because the statements were not prepared following Canadian Public Sector Accounting Standards." She also warned "The Legislature and all Ontarians must be able to rely on the province's consolidated financial statements to fairly report the fiscal results for the year. This year they cannot do so." The AG announced the deficit was understated by \$1.44 billion and the net debt understated by \$12.429 billion, both for 2016-17.

At issue is the government's accounting of the pension fund surplus and "the government inappropriately recording the market account of the Independent Electricity System Operator." Lysyk also warned that the accounting used for the so-called Fair Hydro Plan may lead to a larger understated deficit and debt next year (we first disclosed last March that the government was shifting the costs onto OPG's books). The AG will release a Special Report on this shortly. Significantly misstated.

Minimum wage hike

Last month we saw the Ontario Chamber of Commerce release a report revealing that the proposed 32% increase in minimum wage (by the end of 2018) will put 185,000 jobs at risk. This month, one-after-another, experts weighed-in with their job loss analyses. They all agree on one thing – job losses will be severe – they're just debating how many tens of thousands of people will be affected.

The Legislature's own Financial Accountability Office estimates that Ontario's proposed minimum wage increase will result in a net loss of approximately 50,000 jobs, with job losses concentrated among teens and young adults. They add that "there is evidence to suggest that the job losses could be larger" than their estimate, as the increase is both "larger and more rapid than past experience, providing businesses with a greater incentive to reduce costs more aggressively." They also concluded that "since minimum wage targets low-wage workers, but not necessarily low-income families, raising the minimum wage would be an inefficient policy tool for reducing overall poverty."

The Fraser Institute released their bulletin, *Ontario Enters Uncharted Waters with a $15 Minimum Wage*. They suggest that such a rapid increase in the minimum wage could have harmful unintended consequences, reducing employment opportunities for young and less skilled workers. Their analysis drills deeper into how various regions will be affected when minimum wage passes 45% of the region's average wage – the threshold where negative economic effects grow more severe.

TD Economics published their economic assessment which forecasts "a net reduction in jobs of around 80-90,000 positions by the end of the decade." TD concludes that the "relatively rapid speed of the implementation and its timing within the economic cycle are two factors that will likely accentuate the negative hit to Ontario employment." With respect to the timing, they feel it could coincide with "significantly slower economic growth"; the economy is "likely to endure a cyclical slowdown in both housing activity and household leverage, (and) economic growth will likely slow sharply in the province." As one solution, they suggest "these estimated job impacts could be mitigated by extending the implementation timeline."

The Canadian Federation of Independent Business also issued their research snapshot, *$15 Minimum Wage: Jobs for Canada's Youths at Risk*. Their job-loss number is between 68,100 – 155,900 and "would particularly affect employment opportunities for Ontario's youth, a segment of the population that already suffers from high unemployment."

The Keep Ontario Working coalition released their report, *The Flip Side of "Fair"*, which showcases testimonials from employers outlining how this new government Bill will negatively impact their ability to do business in Ontario. They also released their final economic impact analysis by The Canadian Centre for Economic Analysis. It reveals that if the government were to do nothing other than implement the minimum wage increase over five years instead of the next 15 months, jobs at risk would decrease by 74% in the first two years.

The economy

The government continues to push their $15 minimum wage plan because according to them, the Ontario economy is doing well, and everyone should share in that. Ontario's Labour Minister announced "The prosperity that we're seeing in the Ontario economy now has to be shared by everybody." That's it in a nutshell; this is the government's central rationale.

To push this point, the Labour Minister stood in the Legislature and announced "It's true that the Ontario economy is doing very well; manufacturing exports are up." Except that isn't accurate. A recent headline, "July Trade Deteriorates", leads the story indicating Ontario's exports fell 22% this summer. Stats Can just released their data showing manufacturing sales in Ontario suffered their largest decline in eight years. Then the Minister doubled-down with, "We're leading the G7 in economic growth." Ontario's Finance Minister backed him up with "Ontario is number one in North America when it comes to growth." Except neither of those statements are even close to being accurate. Ontario's growth is not number one; it is tied for 28th place – there are 27 U.S. states ahead of us!

If that wasn't enough, perhaps some of this summer's media headlines will complete the picture.

"Exports Languish"
"International merchandise exports fell, while imports edged higher"
"Manufacturing sales slipped in a widespread decline across industries"
"Retail sales cool"
"Ontario ranks 44th (out of 60) in Labour Market Rankings"
"Once powerful Ontario now a fiscal laggard in Canada"
"Canadian incomes jump; Ontario residents hit by manufacturing downturn"
"Ontario: Fiscal leader to fiscal laggard"

Sadly, the facts don't align with the government's narrative, but that doesn't stop them from continuing to read from their talking points.

The government continues to make fiscal and economic boasts that are not supported by facts. Ontario businesses and families need accuracy to make solid judgments when it comes to making investment and other vital decisions.

October – Making up its own accounting rules

For the second consecutive month, both the Auditor General and the Financial Accountability Office have released very alarming reports about the true state of Ontario's finances.

This is important to acknowledge as the divide between what the independent Legislative officers are presenting and what the government is offering, is growing wider. The numbers the officers are presenting are vastly different than the numbers the government is offering. In accounting, this simply shouldn't be.

Last month, the Financial Accountability Office (FAO) presented a report concluding the government's debt reduction commitment was based on "unlikely assumptions." And the Auditor General (AG) responded to the government's financial statements by issuing a "qualified" audit opinion because, based on the evidence, the statements were "significantly misstated." The government's response, once again, was to attempt to disparage the Auditor General.

This month, further "concerns about fiscal transparency, accountability, and value for money" were presented by the Auditor, with respect to the so-called Fair Hydro Plan.

The issue

As with many reports, the title, *Fair Hydro Plan: Concerns About Fiscal Transparency, Accountability, and Value for Money*, reveals what to expect. If there's any doubt, the opening paragraphs, written by the AG, add an exclamation point: "When governments pass legislation to make their own accounting rules that serve to obfuscate the impact of their financial decision, their financial statements become unreliable." And, "When organizational structures and transactions are designed to remove transparency and accountability, and unnecessarily cost Ontarians billions of dollars, the responsibility of an Auditor General is to apprise the Legislature and the public in accordance with the Auditor General mandate."

At play here is the government's so-called Fair Hydro Plan, announced as a 25% reduction in hydro bills. Over many months we've learned this will cost anywhere between $45 billion and $93 billion, depending on how much the government has to borrow over the next 29 years. That much we knew going in. What the Auditor General has confirmed is that **the government created a complicated financing structure, designed to keep the true cost of the Plan off the province's books, so as not to show a deficit or increase debt. And, that this decision could cost Ontarians $4 billion more in interest costs, as the off-book structure doesn't have the same borrowing power as the province.**

In the AG's Words

It's important to read exactly what the Auditor General wrote, so you can determine just how serious this is, from a financial perspective and a moral/ethical perspective.

The AG opens with "the accounting rules being applied are actually not in accordance with Canadian Public Sector Accounting Standards (PSAS)." As an independent, nonpartisan Office of the Legislature, AG Bonnie Lysyk felt it her "responsibility to speak out when the financial information of the government is not, or will not be, presented fairly and transparently to both the Legislature and Ontarians."

In the Summary of Concerns, we learn that "it is clear that the government's intention in creating the accounting/financing design to handle the costs of electricity rate reduction, was to avoid affecting its fiscal plan. That is, the intention was to avoid showing a deficit in the province's budgets and consolidated financial statements, and to likewise show no increase in the Provincial net debt."

While the AG does not question the government's policy decision to reduce electricity bills, her concerns are that the "planned accounting for the government's budgets and consolidated financial statements is incorrect, and that it was known that the planned financing structure could result in significant unnecessary costs for Ontarians."

The substance of the issue is straightforward. The government has reduced hydro bills, making them lower than the actual cost. However, the power generators still need to be paid, so the government will borrow cash to cover the shortfall. That additional money needs to be accounted for as part of the annual deficit and net debt. However, the AG says "the government did not properly account for this debt … and is not planning to account for it properly." **"In essence, the government is making up its own accounting rules."**

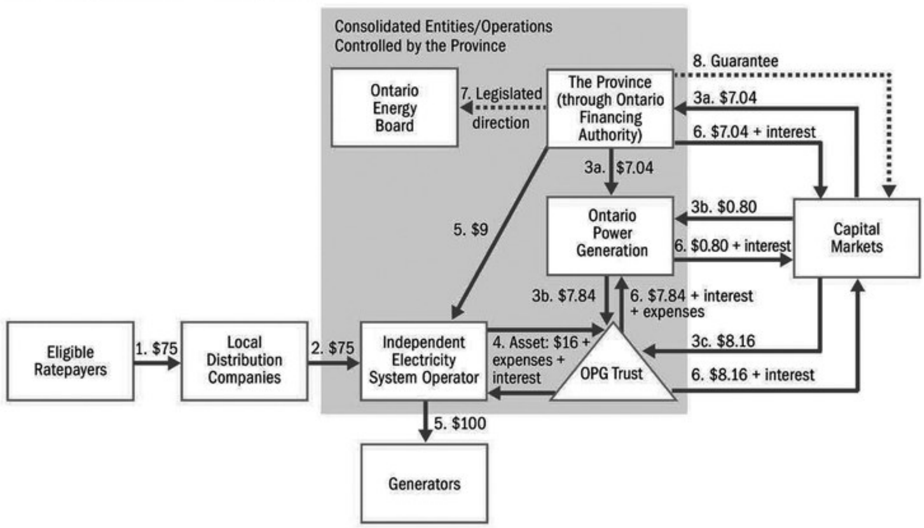
The Special Report adds the following key concerns:

- The government created a needlessly complex accounting/financing structure in order to avoid showing a deficit or an increase in net debt
- To pay back the borrowings, from 2028 on, ratepayers will be charged more than the actual cost of electricity being produced
- Those borrowings are estimated at approximately $40 billion, including $4 billion in extra interest charges (extra because some of the money would be borrowed at a higher rate by OPG)
- They are doing this by creating a 'regulatory asset' (more on that later)
- The creation of a regulatory asset violates the government's own accounting policies developed within Canadian PSAS
- The government knew there was a high risk this would trigger a "qualified" audit opinion, but accepted this risk in order to avoid showing a deficit and an increase in net debt

To summarize the Auditor's report, "the government made a critical decision early in the process of setting out the details of the Fair Hydro Plan: the accounting treatment should not affect the fiscal plan – that is, it should not show any deficit incurred from this required borrowing, nor should it add to the amount the government would report as Ontario's net debt." This was set as the mandate to senior officials and private-sector external advisors, who worked for months to achieve this political goal. In addition, they spent considerable funds; more than $2 million on advisors and a $500,000 legal retainer for a firm to vet e-mails before turning them over to the AG. (They still haven't turned them all over). However, as indicated in the AG's report, the accounting advisors confirmed in discussions that "their opinions regarding the financial reporting of individual entities such as the IESO, OPG and OPG Trust do not extend to the province's consolidated financial statements."

Figure 2: The Form of the Planned Accounting/Financing Transactions

Prepared by the Office of the Auditor General of Ontario



This chart was prepared by the Office of the Auditor General. It shows just how convoluted and confusing the structure developed by the government is.

In the end, the government decided on a very complex form to achieve "the mandate to avoid recording an annual deficit and an annual increase in net debt." The Independent Electricity System Operator (IESO) sells the revenue shortfall to a newly-created OPG Trust as if it was an asset, and pays the power generators their full amount owed. They call the shortfall or net expense, a "regulatory asset". In a complex series of transactions, which the Report carefully outlines over several pages, the AG concludes "the end result of the accounting design is that the financial statements for the IESO, OPG, and OPG Trust, as well as the consolidated financial statements for the province, will NOT show any bottom-line impact for the costs of the government's policy decision." "The 'asset' being legislated into existence does not meet the accounting requirements for an asset on the province's consolidated financial statements, which are prepared following Canadian PSAS." "Accounting that creates an asset to avoid impacting net debt is contrary to the Canadian PSAS framework."

Through legislation, the government created their own accounting asset. They simply legislated the loss at IESO, as a "regulatory asset". If governments are allowed to call losses "regulatory assets", we'll never have deficits again. It's shameful to listen to the government attempt to justify this as some sort of normal accounting procedure. They use U.S. private-sector accounting examples to justify what they did. The U.S. framework is entirely different than Canadian PSAS – we stress net debt; U.S. standards don't have a net debt model. Besides, if the government thought this was OK to do, why didn't they just ask the AG about it in the beginning? Nonetheless, this isn't even an accounting issue – it's a devious political decision. The government had hundreds of people working on this since January, and spent millions, all to concoct a scheme to keep the immense impact of their policy decision off of the government's books. They knowingly risked receiving a "qualified" opinion, and the entire Cabinet knew it would cost several billions more to do it this way, but proceeded anyway.

November – Pulling back the curtain

The main feature this month was the government's *Fall Economic Statement*. The government pitched this year's FES as an olive branch to business in the wake of their change of direction which will now raise the minimum wage to $15 by 2019. This was passed despite warnings from various authorities including the Financial Accountability Office, TD Economics, and the Ontario Chamber of Commerce (OCC). They've all warned that the resulting job losses will be anywhere from 50,000 to 185,000. However, the OCC's research came up with one key finding – if the increase is phased in more slowly, the job impacts would be mitigated by 74% in the first two years. Given the job loss numbers, that's significant, and should be considered.

In the Fall Economic Statement, the government will lower the small business tax rate from 4.5% to 3.5% as an offset. But it's not nearly enough. The Keep Ontario Working Coalition says an accelerated minimum wage hike will have a $12 billion impact on businesses, where the government's remedy attempt will only amount to $500 million.

Here's one real-life example of what this will do. The owners of a mom-and-pop restaurant came into my office and opened up their books. The minimum wage increases will cost them $152,000 annually. That additional cost would eliminate any annual profit and plunge them into a loss. In this scenario of rushing the increase, the government's small business tax rate doesn't help – 3.5% of zero is still zero. This business has already moved to eliminate four positions in anticipation of the government's legislation coming into force in January.

This is typical across Ontario. In fact, a majority of members surveyed by the Canadian Federation of Independent Businesses (CFIB) say they will either increase prices, reduce hiring, or reduce hours, while 43% say they will cut the number of employees in response to the changes. To put this all in perspective, another business owner told me that if the government removed all their HST, EHT, and corporate taxes, that still wouldn't be as much as this additional minimum wage cost.

The government was quick to promote this rate change as something positive, as outlined on page 160 of the *2017 Ontario Economic Outlook and Fiscal Review*. "Internationally, the combined federal-Ontario CIT rate for small business would be the lowest among G7 member countries." The only problem is that there is absolutely no truth to that statement! British Columbia, Manitoba, Newfoundland, Nova Scotia, Saskatchewan, and the Yukon all have lower small business tax rates – Ontario is now simply in the middle of the pack.

Digging into the numbers

Equally concerning with the Fall Economic Statement are the government's fiscal projections. On almost every metric, the government underperformed the targets laid out in the 2017 budget. With the Canadian economic upturn this year, many private sector economists expected GDP growth for Ontario of 3% or better. Yet the government's revised projection is for only 2.8% growth. Total revenue growth since the budget has been only $115 million, but expenses grew by $215 million. A slowdown in housing also reduced land transfer taxes. But despite this dismal performance, the government has not changed its revenue projection of a $10 billion increase this year. That's simply not reasonable.

The government admits Personal Income Tax and Health Tax revenue was down $1.8 billion from the spring budget. As well, the government is now forecasting average revenue growth of 4% over the next four years, while the Financial Accountability Officer says it will be 3%. We're talking about a difference of billions of dollars. The numbers just don't add up and aren't realistic.

TABLE 3.10 2017–18 Revenue Changes since the *2017 Budget*
($ Millions)

	2017–18
Taxation Changes	
Personal Income Tax and Ontario Health Premium	(1,832)
Corporations Tax	1,579
Land Transfer Tax	(270)
All Other Taxes	293
Total Taxation Changes	**(230)**
Government of Canada Transfers	**145**
Income from Government Business Enterprises	**200**
Total Revenue Changes since the *2017 Budget*	**115**

Note: Numbers may not add due to rounding.

Also of note in the FES is that the $1 billion promise for the Ring of Fire infrastructure contained in the 2014, 2015, and 2016 budgets has now disappeared. Interest on debt will rise to $12.2 billion, reaching $13.3 billion in 2019-20. And while infrastructure spending is budgeted at $12.9 billion, more than $6 billion remains unspent over the past three years.

Falling behind

Statistics Canada released census data on income in Ontario, and the numbers are certainly alarming. The Institute for Competitiveness and Prosperity offers the following summary: "The results paint a bleak picture for the progress of Ontario's middle-class over the past decade. Median individual total income in Ontario grew only 3.8% between 2005 and 2015; the lowest growth rate among all provinces and well below Canada's growth of 12.7%." When you look at the median employment income in Ontario over the same period, it decreased 2.3%, the only negative growth rate among all provinces. After-tax income growth in Ontario was less than half of the national number.

Labour force participation, productivity, and income distribution are cited as factors, but the Institute also states "Ontario's contracting manufacturing sector is partly responsible." With more than 300,000 jobs lost in that sector, it seems an obvious point.

Free falling

BMO was blunt in its assessment of the Canadian economy – "Evidence is mounting that the amazing run …from mid-2016 to mid-2017 is over and done." A number of other headlines and commentaries continue to chip away at the false façade the government continues to put up when it comes to the state of Ontario's finances. Among them:

- Scotiabank reports retail sales growth in Ontario declined for two consecutive quarters
- Ontario saw the lowest rate of increase in auto sales among all provinces in October (0.7%)
- BMO Capital Markets reports an "unnerving" four-month slide in export volumes despite a still relatively competitive Canadian dollar
- BMO also cites "uncertainty" in the housing outlook as the Greater Golden Horseshoe works through the impact of the province's housing plan and new OSFI measures

- The Fraser Institute reported 99% of Ontario job creation since 2008 is in Toronto and Ottawa, leaving other areas of the province behind
- BMO says Ontario still looks like the province most at risk from a disruption to NAFTA; Ontario's U.S. exports are 82.8% of its total exports
- Central1 says NAFTA negotiations remain a potential downside risk to the provincial economy long-term
- CFIB's Business Barometer index in October (55.5) is the fifth consecutive month that small business confidence is lower compared to the same month in 2016

The real story on power export losses

The Ontario Society of Professional Engineers (OSPE) laid bare the facts regarding how much the province loses regarding surplus power exported to our neighbours every year. Their study of data from the province's own Independent Electricity System Operator (IESO) found exports of surplus nuclear, wind, solar, and hydro power has cost Ontario up to $1.25 billion from the start of 2016 to the end of September, 2017.

While the government continues to insist hydro rates will fall and the system is reliable, Hydro One confirmed the utility has applied for a 4.8% rate increase "to keep the system stable". In fact, statistics show Ontario has the least reliable system in terms of outages in Canada. According to Eaton Blackout Tracker, the number of Ontario outages increased by 275% from just 2012 to 2015.

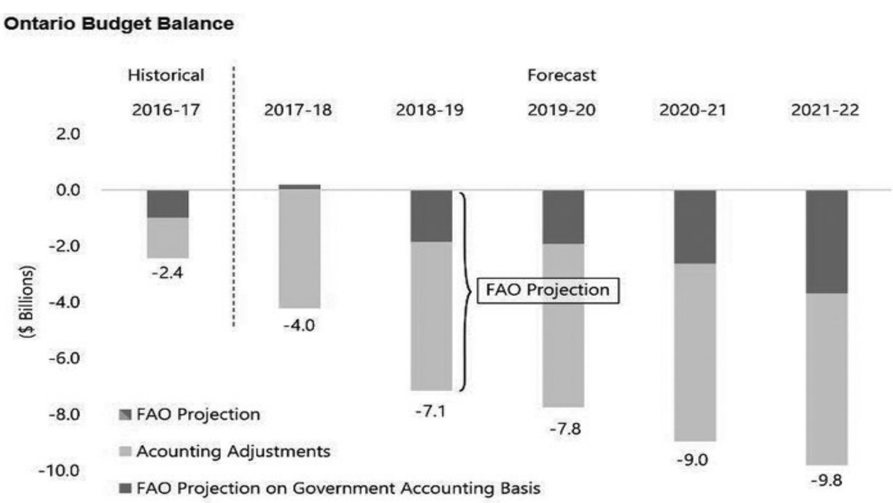
Hydro One also announced its third-quarter profit fell 6% from last year due to the $6.7 billion purchase of U.S. utility Avista.

As the Auditor General and Financial Accountability Office have pointed out repeatedly, the government's financial claims are not reliable. They have refused to alter their bottom line fiscal projections in the Fall Economic Statement, while admitting they have underperformed almost all the fiscal targets laid out in the spring budget to this point.

December – Year-end in focus

Of major significance was the release of the Financial Accountability Office's (FAO) *Economic and Fiscal Outlook: Assessing Ontario's Medium-term Prospects*. The very first sentence should give you all the information you need … "FAO projects a return to significant budget deficits." It goes on to explain that despite a strong boost to revenues this year (much is onetime revenue), "the FAO is projecting a budget deficit of $4 billion in 2017-18." This is the result of the Auditor General's (AG) recommended accounting treatment for both the government's so-called Fair Hydro Plan and the net pension assets of jointly-sponsored pension plans.

Beyond this year, the FAO is projecting a "significant increase in the budget deficit due to the loss of time-limited revenues, a more moderate pace of tax revenue growth, and the growing impact from the Fair Hydro Plan." By 2021-22, the FAO is projecting a budget deficit of $9.8 billion. The report reveals "This is a significant deterioration since the FAO's spring outlook and is primarily the result of the introduction of the Fair Hydro Plan, which will add $3.2 billion to the budget deficit by 2021-22, under the Auditor General's recommended accounting treatment."



Note: Budget Balance before reserve.
Source: Ontario Public Accounts, 2017 Ontario Economic Outlook and Fiscal Review and FAO.

The FAO, both in the report and in the briefing lock-up, expressed concern about having all these various accounting interpretations, leading to several versions of deficit numbers. The report concludes "It is becoming more difficult for legislators and the public to assess the government's fiscal projections. This has reduced the transparency and reliability of Ontario's fiscal plan."

The FAO stated that "additional measures to raise revenue or lower spending will be required if the province intends to achieve and maintain a balanced budget." However, there are major differences between the FAO's forecasts and the government's, both on the revenue and expense side. According to the government, between 2017-18 to 2019-20, revenues will grow by 5.2% on average, much higher than the FAO's projection of 4.3%. This results in a difference of $2.9 billion in tax revenue. In addition, many of the one-time revenues will expire, including federal equalization payments (gone by 2019-20), debt retirement charge, federal infrastructure transfers, carbon allowance proceeds (there were five auctions vs four as in most years), and sales of assets, such as Hydro One and various real estate. On the expense side, the government will spend $9.7 billion more than what they had planned to spend in 2017-18, according to their own fiscal plan of just two years ago.

As for the key risks in the outlook, the FAO, as well as most forecasters, continues to assume that uncertainty over NAFTA will have a detrimental effect. Some businesses are postponing investment decisions until this is resolved. The FAO is also concerned that "strong growth in household spending has not been matched by similar gains in household incomes, leading to higher levels of household debt." With rates expected to rise, "many households will scale back discretionary spending in order to make higher debt interest payments, which in turn could have implications for the pace of overall economic growth." In the FAO's spring report, it outlined the housing market as a significant threat to the economy, with record consumer debt loads and stretched level of affordability.

Further analysis

This all ties in with what many associations and financial groups published in December. RBC Economics stated "After several years of consumer spending and housing activity acting as the main engines of growth, changes to regulations in the housing market and rising interest rates are setting up for a moderation in housing resales and ancillary purchases." With respect to overall growth, RBC further commented that "economic slack has diminished considerably following long periods of expansion, making it harder to repeat 2017's rapid growth rates."

Central 1's economic analysis sees slower growth in the near term, largely from personal consumption and residential spending, with a small drag from a shrinking trade balance. They also list the minimum wage impact and NAFTA uncertainties as sources of risk for the province's economy. Central 1 also reported that small business optimism in Ontario decreased since November, to 57.5/100 (down 0.8%). Since June, year-over-year small business confidence tracked lower than the same period last year. December's year-over-year negative gap was the widest of 2017.

Many organizations chimed in on the minimum wage issue. The Bank of Canada announced that Ontario's move to $15 per hour will cost the province 60,000 jobs. This is bracketed by the Financial Accountability Office's estimate of 50,000 lost jobs, and TD Bank's assessment pegging it at 90,000 jobs to be lost. The CFIB suggested this change will cost Ontario between 68,100-155,900, when both direct and indirect job losses are considered. Undoubtedly this debate will continue, but all eyes will be on the monthly labour statistics, for some months to come.

In a series of blistering reports, the Fraser Institute painted a bleak picture of Ontario. The titles are very revealing. *Uneven Recovery: Much of Ontario still hasn't fully recovered from the 2008 recession; Canada's job engines are in the West and Quebec – not Ontario; Ontario's manufacturing sector falling behind other provinces, U.S. states;* and *Rising electricity costs and declining employment in Ontario's manufacturing sector.*

Fraser claims that most of the province's job creation took place in its largest urban areas. Toronto and Ottawa alone created the equivalent of 98.6% of all new jobs in

Ontario between 2008 and 2016. Basically, throughout the rest of Ontario, there has been virtually no job creation since 2008. I can attest that my hometown of North Bay is one of the 17 urban areas that are under the national average, and one of the 11 urban areas that actually experienced net job losses (around 9%) since 2008.

While Ontario is not alone in having a reduced manufacturing sector, it exhibits the most substantial decline when compared to other jurisdictions in Canada and the U.S. Fraser compared the manufacturing sector's share of real GDP between 2005 and 2016. Ontario's share dropped 5.1% compared to the U.S. falling less than 1%. In fact, several jurisdictions in the U.S. northeast (our main competitors) saw increases, including Indiana at 1.5%, and Michigan and Kentucky by almost 1%. Another indicator of decline is Ontario's relative ability to attract investment. Between 2006 and 2016, manufacturing investment declined by 26%, while it increased in Saskatchewan by 35%, B.C. by 15%, Quebec by 11%, and Manitoba by 5%.

The various reports conclude "Ontario is faring so poorly relative to other jurisdictions that all face the same challenges. Simply put, poor policy, including policies that have dramatically increased electricity costs, which have likely placed too large a financial burden on manufacturing and hampered the sector's competitiveness."

Hydro still making news

Ontario's skyrocketing hydro rates just can't seem to shake the news cycle. You'll read in the next chapter details of the Auditor General's revelation that $260 million was paid out in ineligible expenses claimed by power plants. Opposition parties have called for a deeper review, including asking the OPP to investigate. It was further revealed that Ontario Power Generation is one of the companies that still owes ratepayers for inappropriate expenses.

New government rules forced local utilities to promote the government's programs. An Order in Council mandated that utilities must print 'Ontario's Fair Hydro Plan' and 'Bringing electricity bills down' in a "reasonably prominent location on the face of the bill insert." The so-called Fair Hydro Plan is the name the government gave to their financing scheme to temporarily (and the AG states artificially) lower hydro bills by an average of 25%. The Niagara-on-the-Lake Hydro Board issued a statement accusing the government of politicizing electricity bills.

Hydro customer debt and disconnections soared, according to new numbers quietly posted by the Ontario Energy Board. During the past four years, there's been a 19% increase in residential hydro disconnections, a 28% increase in households in arrears, and a 40% increase in customer debt owed to the local electricity distributors. North Bay Hydro wrote off more than $1.12 million in past-due bills for 2,930 customer accounts. This was 40 times greater than the $25,573 written off the previous year, for 145 accounts.

A CBC News story detailing how market-based bidding has pushed down the price of renewable electricity in places such as Mexico, got others doing comparisons with Ontario's costs. The story described 'the cheapest electricity on the planet' in Mexico, at 1.7 cents/kwh for wind power. Over the last year the rate paid to wind generators in Ontario was 14 cents/kwh. As a result, Ontario families and industries are struggling to pay amongst the highest all-in electricity rates in North America, with rates increasing by 71% since 2008.

Ontario families, businesses, Legislators, and rating agencies, need to trust the government's fiscal projections. But as the FAO stated, there is reduced transparency and reliability of Ontario's fiscal plans. This needs to end. We should have one set of books in Ontario – and a government that will work to ensure the government's books are properly reported.

The major financial news in December of every year is the release of the Auditor General's (AG) Annual Report. As with last year, the AG had another very impactful year, offering a serious look at how the government spent our tax dollars – and how they accounted for the spending. In February, Bonnie Lysyk said "Show me the letter", referring to a letter she wants to see from OPSEU and the Ontario Teachers' Federation allowing the government to record any pension surpluses onto the government's books. In May, she spoke to the committee reviewing the Ontario Fair Hydro Plan Act, and suggested that the government's Act is not in accordance with Canadian Public-Sector Accounting Standards (PSAS). In September, the Auditor issued a *qualified* audit opinion, "because the statements were not prepared following Canadian PSAS." She added that the statements "significantly misstated" the province's deficit as well as net debt, due to the pension and hydro issues. Finally, in October, she issued the following Special Report, *The Fair Hydro Plan: Concerns About Fiscal Transparency, Accountability and Value for Money.* She opened with, "The government's structure will hide from Ontarians the real financial impacts of its electricity rate reduction."

Now, we have the Auditor General's 2017 Annual Report. The title of the News Release sums it up … ***2017 Annual Report Identifies Need for Better Government Planning to Act on Known Issues.***

The two-volume 1,119 page Annual Report contained value-for-money audits of provincial spending in agriculture, emergency management, energy, health care, education, services for newcomers, government-owned real estate, and social housing.

There are some real eye-openers again this year. School board employees are taking extra sick days, hydro customers are paying more because energy producers were gaming the system, and, no surprise here, the books aren't really balanced!

But the standout this year was a blistering indictment of the Independent Electricity System Operator (IESO) and their costly administering of the Standby Cost Recovery Program. This plan allows several gas and coal power generators, whose equipment needs to be warmed up, running and ready to go should the IESO need electricity quickly, to be paid for being on standby. The electricity market consists of 560 companies that either generate, export, or distribute electricity. Together, they were paid $17.5 billion in 2016. Over the last 11 years, nine companies enrolled in the Standby Cost Recovery Program claimed $600 million in compensation, but the audit found almost $260 million were for ineligible costs.

Only fuel, maintenance, and operating costs that generators incur for being on standby are eligible. But the IESO was not reviewing all the cost claims before paying. As a result, generators claimed thousands of dollars annually for staff car washes, carpet cleaning, road repairs, landscaping, scuba gear, and raccoon traps. All had nothing to do with running their power plants. One generator claimed $175,000 for coveralls and parkas, over a two-year period.

The Auditor singled out Goreway Power Station for particularly egregious activity. The Auditor stated that $17 million in costs were claimed for which it could not provide any supporting records. An extra $25,000 was claimed each time they started their equipment, resulting in $5 million in total payments. Ineligible costs were claimed that included $6.5 million for gas to fuel a steam turbine that doesn't consume any gas! The Auditor said they charged (and were paid) $300,000 for landscaping and they provided documents containing fictitious costs – some related to $27 million in equipment parts they had no intention of purchasing and that would be redundant!

The saddest part in all this is that the foxes were running the chicken coop. These very generators who were gaming the system, are the same generators the IESO has on their Market Renewal Initiative panel – to "address known issues with the current market design." And in the 'no surprise' department, one of the Co-Chairs of the Initiative, is a senior representative of Goreway! You can't make this stuff up.

In the Auditor's section on the Public Accounts, again, the title says it all… **Government Financial Statements Becoming Increasingly Unreliable.**

The government's continued use of nonstandard accounting could throw off the accuracy of the province's bottom line by up to $4.5 billion next year, according to the Auditor General. "There is a very real risk that the balanced books expected to be reported by the government using these accounting methods next year will conceal the true annual deficits and net debt." "This will seriously distort the true state of the province's finances."

The AG also cautioned of another issue, and that is whether the government will present a Pre-election Finance Report, as required by law. The Auditor is to review the Report to determine whether it is reasonable, and release a statement before the general election, scheduled for June 7, 2018. However, this can only occur once the government passes a regulation confirming it will release the Report by a committed deadline, something that has yet to happen. I have written to the Finance Minister asking him to assure the Legislature has such a report. (As this book is heading to the printer, we have been informed the AG will release a report before the election).

Here, in the Auditor General's own words, are the independent analyses of the various ministries and agencies she reviewed.

Provincial tribunals

"Large backlogs mean long delays for property owners awaiting Board decisions"

The Assessment Review Board hears appeals about assessments by the Municipal Property Assessment Corporation. Despite a decrease in the total number of appeals it received, they still have a backlog of over 16,000 unresolved appeals. The Ontario Municipal Board hears appeals related to land-use planning matters. They scheduled only 44% of minor-variance cases within 120 days, well below their target of 85%. For complex cases, appeals took between 10 months and seven years to close.

Cancer treatment services

"Most cancer patients' needs being met – with exceptions"

The limited capacity for stem cell transplants requires sending patients to the U.S. costing $660,000 – vs $128,000 average cost in Ontario. The full cost of cancer drugs is not covered unless administered in a hospital. Four provinces provide full coverage for all patients, even if they're administered at home. Wait times for transplants using a patient's stem cells ranged between 234-259 days; 1.5 times longer than Cancer Care Ontario's targets. With donated cells, times were up to 285 days; seven times longer.

Emergency management

"Ontario is not fully prepared to respond to large-scale emergencies"

Emergency plans have not been updated in years, and practising is not frequently done. In fact, Cabinet's EMC hasn't met on this for several years. The last risk assessment was done based on emergencies experienced up to 2009. The Emergency Response Plan and the Nuclear Response Plan have not been updated since 2008 and 2009 respectively. In 2009, Emergency Management Ontario attempted to develop and implement a province-wide IT system but discontinued it in 2015 after spending $7.5 million.

Agriculture support

"Some farm support programs not meeting farmers' needs"

Only one of three main farm support programs provide effective and timely assistance to Ontario's 50,000 farms. The $100-million-a-year Risk Management Program often pays famers with little regard to individual need; only half who received payments between 2011-2015 actually reported a loss or drop in income. Agricorp, the administering provincial agency, has one IT system that is 25 years old and another that is 10 years old, resulting in 31 system-related errors regarding information and payments.

Electricity costs

"Lack of action by IESO costs ratepayers millions"

As detailed in the opening paragraphs, the Independent Electricity System Operator has not implemented important recommendations that could have saved Ontarians millions of dollars on their power bills. In addition to the amounts previously outlined, two programs continue to pay gas generators $30 million annually, more than necessary. A gas generator who misused another program received $20.4 million over eight months and had to return half the overpayment.

Laboratory testing

"Province missed out on millions in laboratory savings"

Ontario could have saved millions of dollars on lab tests if they had updated the nearly 20-year-old price lists it pays private-sector labs for testing. Technological advances have reduced lab-testing costs resulting in a new price list. Had the list been in effect in 2015-16, the Ministry would have saved $39 million in that year alone. The province can save money by conducting more in-province generic testing, as opposed to the $120 million U.S. spent on 54,000 specimens sent out of the country between 2011-16.

School funding

"School board funding formula last fully reviewed in 2002"

In 2002, it was recommended to the Ministry of Education that it annually review and update the benchmarks in the funding formula for school boards. They were also advised to do a more comprehensive overall review every five years. Fifteen years later, the Ministry has not reviewed the funding formula. Had these reviews occurred, they would have learned that special-education funding is not being distributed where it's needed and that $111 million would have been dispersed differently.

Generic drugs

"Room for more savings on generic drugs"

The Ministry of Health is spending more than it needs on generic prescription drugs. While drug prices in Ontario have dropped significantly in the past 10 years, the province still pays more than foreign countries. In 2015-16, Ontario paid $100 million more (or about 70%) for the same drugs as New Zealand. In another sampling of common generic drugs, the Ministry paid $271 million (or about 85%) more than some Ontario hospitals.

Health units

"Success of public health programs in preventing chronic diseases unknown"

The province doesn't know whether our 36 public Health Units are making progress in the fight against preventable chronic diseases. Ontario spends $190 million on preventing diseases, but it does not measure performance of Health Units in this area. And while four modifiable risk factors that contribute to chronic disease – physical inactivity, smoking, unhealthy eating and excessive alcohol consumption – cost Ontario $90 billion between 2004-2013, the number of people living with these diseases is rising.

Infrastructure Ontario

"Government pays millions for hundreds of buildings that sit empty"

Ontario paid almost $19 million in 2016-17 to operate and maintain 812 vacant buildings across Ontario; 600 of them unoccupied an average of eight years. Deferred maintenance of government-owned buildings more than doubled between 2012-17, from $420 million to $862 million. As a result, over the last six years, the average condition of government properties has deteriorated from excellent to almost poor. And by reducing the square footage of its office space the standard 180-sq.ft./person, they could have saved $170 million a year.

School boards

"Employee sick days up significantly at school boards"

School boards are struggling to effectively manage employee attendance. Between 2011-16, boards experienced added financial pressures because of an increase in sick days by their employees. During that period, total sick days increased 29% (from nine to 11.6 days per employee), and the overall sick leave paid as a percentage of payroll increased 25%. This occurred following a centrally-negotiated contract that changed sick-leave policy so that employees could no longer bank their sick days.

Newcomers

"Ministry settlement funding for newcomers needs better oversight"

Of the $100 million the province paid community organizations to provide newcomer services in 2016-17, about $30 million was for services to individuals who were also eligible for similar federally-funded services. As well, funding allocations should be determined based on the relative need for each service. For instance, enrolment for language training declined in each of the last five years, resulting in spending on language training totalling $24 million less than budgeted.

Social housing

"Social and affordable housing needs growing, while supply has been declining"

There are more households on waiting lists for social housing than there are actually living in social housing. The wait list represents about 185,000 households, however since 2004, only about 167,000 households on average have received social housing annually. The Auditor also pointed out that there is no strategy to address the growing social housing wait lists. Social housing is provided on a first-come, first-served basis rather than on assessed need.

Government advertising

"Government spending on advertising is at a 10-year high"

The government spent over $58 million on advertising in 2016-17 – and 30% of that was for ads that appeared intended to make the government look good. This is the highest spending by the government on advertising since 2006/07, and it included millions on ads that would not have cleared under the old Government Advertising Act. Examples include a $330,000 radio campaign that referred to opposition-held ridings and $1 million on their 25% electricity discount, even before it was passed in the Legislature.

Follow-up reports on previous value-for-money audits

"Some progress made toward implementing actions recommended – but they fully implemented only 33% of them"

Some highlights include:

- Little progress by the Education and Transportation ministries on close to 40% of recommended actions with respect to the safe transportation of students to and from schools;
- Implementation by Northern Development and Mines of just 32% of recommendations relating to abandoned mines at a high risk of posing a threat to human health and safety or to the environment;
- While 73% of Long-Term-Care Home Quality Inspection Program recommendations were either fully-implemented or in progress, little or no progress had been made on the remaining 27%, which are important, as the number of complaints and critical incidents at the homes rose 37% between 2014-16.

Here is the conclusion I wrote in the chapter of the AG's Report in last year's *Focus*. You be the judge and see if anything changed:

When the government writes a cheque, the people of Ontario expect their government to ensure they are getting value for their dollar.

Unfortunately, this Auditor General's Report lays out a blistering indictment of this government's waste, mismanagement, and scandals. It paints a picture of a tired and negligent government, incapable of successfully providing even the most basic services. Finally, we saw far too many examples of a government doing what's in their best interest, not in the best interest of the people of Ontario. Capitalizing on the changes to the advertising rules the government brought in last year, and spending millions on self-congratulatory ads, is a prime example.

January 2018 – Minimum wage; Maximum trouble

The new year saw Ontario raise its minimum wage to $14 per hour from $11.60 and plans to increase it to $15 in 2019. This is an increase of about 23% and 32% respectively. The rate increased from $11.40 to $11.60 in October, 2017.

The Bank of Canada reacted with a warning that 60,000 jobs would be lost over 2018 as a result of the minimum wage increase. Their announcement follows earlier job loss predictions of 50,000 from the province's own Financial Accountability Office (FAO), 90,000 from TD Bank, and up to 185,000 from the Ontario Chamber of Commerce. Spoiler alert: early in February we learned that the January numbers from Statistics Canada showed Ontario did indeed lose 51,000 jobs in the month – the largest monthly drop for the province since 2009.

Sadly, this should come as no surprise. In addition to the FAO and others who provided job loss estimates, multiple stakeholders and associations spent months trying to explain to the government how this rapid hike would have an adverse impact on businesses. These groups all attended Bill 148's all-Party public hearings and pleaded with the government to slow the pace to get to $15.

The Canadian Federation of Independent Businesses (CFIB) shared their members' plans to cope with the impacts. 54% said they'd reduce or eliminate plans to hire new workers. 51% said they'd be forced to raise prices. 50% said they'd reduce or eliminate plans to hire young workers. 44% would delay expansion plans.

As forecast, there are media stories about businesses, from manufacturers and retailers to grocers and restaurants, all raising prices. Many businesses have reduced staff in a move they say is necessary just to stay open. And more retailers are automating their check-outs to further reduce staff. The most troubling stories are of the many small businesses that have closed – local newspapers from all across the province have shared stories of long-surviving businesses closing up shop; the minimum wage hike Bill being a bridge too far.

In addition to the hike in minimum wage, Bill 148 has sick pay and leave provisions, as well as new rules on how statutory pay is calculated. It requires all employers to provide staff with 10 days of personal emergency leave each year, including two paid days off. It will also require companies to pay part-time and casual workers at the same rate as full-time workers if they are doing similar jobs.

Many public-sector organizations are also feeling the impact. The Ontario Hospital Association warned it would face $100 million in extra costs from the labour reforms and are asking the province to make up the difference. Frontline public-sector agencies such as Community Living shared the sentiment and have already had huge staff reductions across the province.

The effects of the increase will have a drastic impact on school bus companies as well. The increase in minimum wage and the new provision for guaranteed minimum daily hours for part-time workers could push the costs on operators up by as much as 36%. In response, the Ministry of Education announced $60 million in additional school bus funding. The list of affected groups is endless, all because the government failed to fully-understand the consequences of their actions.

Craig Alexander, Chief Economist of the Conference Board of Canada, was the 'expert witness' the government chose to represent them at the all-Party pre-budget hearings. Here is what he had to say about the minimum wage, to TVO's The Agenda:

"I think it's going to be a big shock to businesses because of the speed at which the minimum wage is going up. I think we could have gone to $15 an hour over a longer time frame and had more of a chance for businesses to adjust to the higher labour compensation. But our modelling, we produce detailed economic forecasts for Ontario, the models would say that the Ontario economy is probably going to lose 42,000 jobs out of the increase to the minimum wage as businesses reduce the amount of labour that they're willing to hire. That doesn't mean employment is going to fall; its 42,000 jobs that would have otherwise been created. Businesses will likely adjust their business model over time as people leave the company, retire etc., they'll adjust their pay scales. Employment in Ontario is going to rise, but it's going to be a significantly slower growth rate as businesses adjust to the rapid increase in the minimum wage." At the pre-budget hearings he reiterated his position. "We can stick to the commitment to going to $15. I would rather see that next stage delayed to give businesses more chance to adjust."

Former government Finance Minister Greg Sorbara was equally critical on the same TVO appearance: "I think it's going to have a very negative effect on the economy. Quietly, businesses are going to adjust by moving to technology, laying people off, curtailing hours, and in many parts of rural Ontario, businesses will just close, because they can't absorb it. If you want to deal with poverty, deal with poverty. Do it through a guaranteed annual income, do it with income supplements, don't put dealing with poverty on the backs of businesses."

Hearing from the experts

Every week in January, an association or major stakeholder group produces a forecast or report on Ontario's finances. Each year starts off at a breakfast with the economists of the five major banks. Most of the banks forecast Canada's growth in the 2% range, while one said 2.4%.

RBC's Craig Wright saw Canada (and by extension, Ontario) headed "in the wrong direction" when it comes to deficits and tax increases. He said that we are getting "less competitive". And when it comes to carbon revenues, the "provinces see (them) as a cash cow." This echoes his comments of last year where he stated that any carbon tax should be revenue neutral – that is return all the revenue to families to cope with the higher cost of living it causes.

BMO's Doug Porter says we face three big risks – NAFTA, the housing market (specifically Ontario, where there was a 12% price retreat in Toronto last year), and "competitive challenges" such as the U.S. tax cut at a time we're not following along and adding a minimum wage increase in Ontario. He also noted that business confidence is at its lowest level in nine years.

Avery Shenfeld of the CIBC said right now is probably as good as it gets, with the 2019 outlook not as good. He ended with "enjoy it while it lasts." TD's Beata Caranci talked about risks to our growth, including NAFTA and the tax cuts passed in the U.S., while Scotiabank spoke of global markets.

The Legislature also holds pre-budget consultations in January, where all three political parties travel the province together to hear from the public. Mostly it is stakeholders who attend but the Legislature hosts one session of experts to describe their take on the state of the economy.

The experts agreed Ontario's growth would be in the 3% range. It has been driven by consumer spending and real estate which is concerning because neither are sustainable. To that point, the Financial Accountability Office (FAO) released *Assessing Ontario Households' Debt Burden and Financial Vulnerability*. The title alone should scare you! The FAO estimates that, for the average household, annual debt payments will increase by $3,000 to $15,500 by 2021. If interest rates were to rise 100 basis points higher than projected by 2021, average debt payments would increase by a further $1,000 per household, equivalent to about 1% of household disposable income. This would likely force households to scale back spending on goods and services and could have significant negative implications for the broader economy. In particular, low-income households, which spend nearly a third of their income on debt payments, will be disproportionally impacted from the rise in interest rates. A rise in rates will also add to the cooling in real estate, down 9.5% last year from 2016's record highs. Adding to that are new requirements for income stress tests when applying for a mortgage. Of note; Ontario saw the second straight quarterly double-digit decline in real residential construction.

Craig Alexander, Chief Economist at the Conference Board of Canada, had these further thoughts which may explain both the consumer spending and the lack of business investment. "Beyond NAFTA, I think businesses are concerned about the rise in minimum wage rates, some of the new labour law regulations, and high electricity prices. There are a number of events in recent years that have more businesses worried about competitiveness, and that's actually getting picked up in our survey of business attitudes." Digging deeper, he added, "I think high electricity prices in Ontario are a challenge for households but they are at a competitive disadvantage for Ontario businesses. We went from a jurisdiction where Ontario actually had cheaper-than-average electricity prices in North America to being the most expensive jurisdiction in North America. Electricity is a core input, so at the end of the day, you want to have competitive and reasonable electricity prices. This is something that shows up regularly in the surveys as a complaint by business."

Exports and investments are where Ontario needs to see growth. That too is problematic, as exports are not rising at the pace we need, and we're losing market share. Exports to the U.S. are still trending down year-over-year for the fifth month in a row (latest data was Nov. 2017) and real international exports fell 9% in Q3. Businesses are only building to sales capacity – they're responsive, not ambitious. They claim that government policy is dampening business's intention and willingness to invest. They also add uncertainty from NAFTA, loss of competitiveness from the minimum wage hikes, and rising interest rates as reasons for holding back.

Interestingly, the Business Development Bank of Canada pronounced that "Canadian business owners plan to boost investments in 2018 to $140.5 billion." By region, BC is planning for a 15% increase, Alberta up 12%, Quebec up 11%, while Ontario businesses expect to trim investments by 1%. This does get lost in the blips of good news. For instance, NOVA chemicals announced their decision to invest $2 billion into their Sarnia-Lambton operations. While this is great news, Ontario is still not winning its fair share of investments. According to the Chemical Industry Association, based on historical trends, Ontario should have seen a further $8 to $10 billion worth of investments, which means we're missing out on decades of additional jobs, tax revenues, and community investments.

You would certainly never know the true state of Ontario's finances by reading the government's Ontario Economic Accounts. They boasted that "Ontario's economy continues to grow", touting an anemic 0.3% growth in 3rd quarter GDP (one-quarter of the 2017 first-half average). They did admit to a decline in exports but blamed that on "extended seasonal shutdowns for retooling at assembly plants." And you certainly wouldn't know the true state of our finances – or the auto sector, from the Premier. She tweeted her boast about supporting the auto sector, showing a video of Camaros rolling off the line. The trouble is the Camaro hasn't been manufactured in Ontario for two years; they are now built in Michigan! That encapsulates the sentiment I express in the other 100+ pages of this book!

Other headlines

- Auto insurance rates in Ontario went up a full per cent in the 4th quarter of 2017… meaning rates are down only 5.5% from 2013. Recall the "stretch goal" where the government promised to reduce rates by 15% by August, 2015?

- Ontario Power Generation was ordered by the Ontario Energy Board to cut $500 million from its nuclear operation costs, disallowing some proposed costs for compensation.

- Hydro One has spent nearly $5 million to redesign customers' bills, with plans to spend another $10 million-plus on future changes.

- If Ontario were its own country, Ontario's top combined personal income tax rate of 53.5% would be second highest of any country, behind only France.

- Between 2001 and 2016, Ontario's inflation-adjusted GDP per person increased at an average of just 0.6%, compared to 1.1% in the rest of Canada as a whole. Ontario's average annual rate of job creation was higher than just two other provinces – Nova Scotia and New Brunswick.

- Ontario will receive $21.1 billion in federal transfer money this year; a 48% increase in eight years. Ontario is also receiving $1.4 billion in equalization money this year, and will receive equalization again in 2018-19, continuing its status as a 'have-not' province.

- Contrary to the claims that Ontario leads the G7, Scotiabank says "Alberta and BC will lead the pack" in 2018 and 2019 in GDP growth among provinces.

- Ontario announced a $784 million plan to fix 79 schools, when the estimated repair backlog is $15 billion among 4,900 schools.

- "Repairs to a bridge in Northwestern Ontario will take nearly three years and delays have pushed the total cost well over the initial $8 million to $12 million estimate.

February – Not so rosy

Three key reports from the Ontario Chamber of Commerce (OCC), the Financial Accountability Office (FAO), and the Fraser Institute revealed further contradictions to the rosy narrative being painted by the government.

The Ontario Chamber of Commerce presented their *2018 Ontario Economic Report* (recall their report used to be entitled *Emerging Stronger*). This comprehensive analysis of data and emerging trends on the economic health of the province shows business confidence in the province continues to drop. The number one reason, cited by three-quarters of those surveyed, is the Ontario government's economic policies. In their formal news release, the Chamber highlighted the following areas of concern:

- Businesses are losing confidence in Ontario's economy. In 2012, 47% of businesses reported they were confident in Ontario's economic outlook. Today, that share has been halved, as only 23% of businesses are confident in the economy.

- Nearly two-thirds of businesses cite input costs for their lack of confidence, such as the price of electricity, taxes, and the increase in minimum wage. This is compared to only 31% who name competitive barriers such as declining consumer demand or changing client behaviour.

- One quarter of small businesses in Ontario project declining revenue in 2018. That's twice the rate of large firms (26% vs. 13%). Given that the majority of businesses in this province are small, this will likely have a net-negative impact on economic growth.

- The production of goods and services represents a shrinking contributor to business prosperity. Production activities represent only 15.3% of business prosperity, meaning that prosperity is increasingly becoming more dependent upon financial activities instead of productive activities. This is indicative of Ontario possessing a higher-risk operating environment.

- Our historically low unemployment rate is a red herring, as more individuals remove themselves from the workforce or simply give up the search. The percentage of Ontarians not participating in the labour force is at a recent high of 35%, contributing to employers' on-going struggle to attract talent.

"Industry in Ontario are feeling the impact of the rising minimum wage, significant labour reforms, increasing global and U.S. competition, NAFTA negotiations, consistent overregulation, rising input costs, and challenges to accessing talent," said Rocco Rossi, President and CEO. "(There have been) significant changes that taken as a whole leave Ontario as the second most expensive jurisdiction in North America on a combined tax basis, second only to Nova Scotia ... and that is critical in terms of decisions around investment and around an ability to compete."

FAO – Hydro One

The very first report produced by the new Financial Accountability Office (FAO) was a financial analysis of the sale of Hydro One. Now that reality and the figures have set in, the FAO provided their *Updated Financial Analysis of the Partial Sale of Hydro One*. To no one's surprise, it confirms what we have been professing from day one – one-time funds have been used to artificially balance the Ontario budget.

In December of 2017, the Province of Ontario completed its final sale of Hydro One shares, generating an estimated $9.2 billion in proceeds from selling 53% of Hydro One. The FAO estimates that Ontario's balance sheet will improve by a total of $3.8 billion over the fiscal years 2015-16 to 2017-18 from the one-time gain from the sale. For fiscal 2018-19, they FAO estimates the finances will deteriorate by $1.1 billion. And from 2019-20 to 2024-25, the balance sheet will deteriorate by an average of $264 million each year. The negative impact results from the lost share of 53% of the annual net income from Hydro One.

Right from day one, the FAO stated that if this sale was nothing more than generating revenue for infrastructure development (as the government stated) then they should borrow instead. They take that a step further in this report, by actually developing an alternative financing scenario. The FAO proved that as a result of the sale, net debt will be higher, and it will cost the province $1.8 billion on a discounted cash flow basis, when compared to alternative financing an equivalent amount of infrastructure investment by issuing provincial debt.

Remember, the government insisted, over and over, that the sale of Hydro One was to pay for infrastructure investments. However, the FAO uncovered that "through 2017-18, it is expected that only $670 million in infrastructure project spending connected with the Trillium Trust commitment will have occurred." So not only have these billions not been spent on infrastructure, the FAO says the timing implies that "the province will experience a positive fiscal impact through 2017-18, but a growing negative impact as more infrastructure projects are expensed."

FAO – Labour market

The Financial Accountability Office (FAO) also reported on the state of Ontario's labour market and found many troubling trends. They included:

- Many labour market indicators such as the share of full-time and private sector employment have yet to recover to their pre-recession averages.

- The pace of job growth has been uneven across Ontario regions. Job gains in 2017 were heavily concentrated in the GTA (+69,700 jobs) and Central Ontario (+57,200 jobs). Only 1,600 net new jobs were created in Southwestern, Eastern, and Northern Ontario combined.

- The number of Ontarians experiencing long-term unemployment remains above the pre-recession level.

- Wages grew very slowly in 2017, continuing the trend of weak wage growth since the 2008-09 recession.

- The labour force participation rate of Ontario youth remains well-below its historical average.

- Average wages increased by only 1.1% in 2017, the weakest gain since 1998.

- In January 2018, total employment fell by 51,000 positions compared to December (on a seasonally adjusted basis), with a drop in youth employment accounting for roughly half of the overall decline. Total part-time employment fell by 59,000 jobs in January, more than offsetting a small gain in full-time employment.

- Ontario's Gender Pay Gap Did Not Improve in 2017

- Non-standard forms of employment – sometimes referred to as 'precarious work' – have become more common. The share of temporary workers and multiple job holders (relative to total employment) increased in 2017, continuing a rising trend since the late 1990s.

Repeating past mistakes?

With pre-election spending topping $7 billion, the highest since the 2009 recession, the Fraser Institute penned *Repeating Past Mistakes? Spending Restraint Critical for Ontario's*

Fiscal Health. It is described as a wake-up call that if left unanswered, will leave Ontario's finances vulnerable. Here are their specific points:

- In 2016-17, Ontario's net debt reached $302 billion, or approximately $21,500 per Ontarian. The province's debt-to-GDP level stands at 38%, just below its all-time historic high.

- Ontario's net debt has increased dramatically since 2003-04, with the province running budget deficits in 11 of the past 14 years. These annual deficits have ranged from $991 million to $19.3 billion and have averaged $8.6 billion over the whole period.

- The provincial government's spending choices are a primary cause of Ontario's persistent deficits. Between 2003-04 and 2016-17, provincial program spending increased at an average annual rate of 4.9%. This rate of growth greatly surpassed the province's overall rate of economic growth (3.5%) and the rate that would have been required to offset the combined effects of inflation and population growth (2.8%).

- If the government had restrained program spending growth to the rate of nominal GDP growth since 2003-04, the province would have run budget surpluses every year since 2004-05; the large run-up in provincial debt since 2003-04 would not have occurred.

- Between 2003-04 and 2010-11, spending increased quickly, followed by a period of significantly slower spending growth between 2011-12 and 2016-17. This slowdown in spending growth, coupled with strong growth in revenues, contributed to deficit reduction in recent years.

- However, the government's 2017-18 budget announced a substantial spending increase for the current fiscal year, suggesting that the short-lived era of comparative restraint may be ending. The Ontario government appears

> to be repeating the mistakes of the past and may once again be exposing the province to substantial risks including the re-emergence of large budget deficits should another fiscal shock occur.

Program spending is up by more than $7 billion this year, or 5.7% – more than three times higher than the average increase in the years following the 2009 recession. In fact, over the last 14 years, program spending – excluding debt – increased from $70 billion to $130 billion, an 84.6% increase, almost double the 44% growth necessary to offset inflation and population growth. When referring to big spending increases that led to deficits and mounting debt the Fraser Institute added that "it is worrying to see the province taking the very same risks all over again."

None of this helped Ontario's economy grow as it should, and as the rest of Canada did. From 2003 to 2015, inflation-adjusted per-person economic growth in Ontario averaged 0.5% annually, about half the growth rate of the rest of Canada.

Other Headlines

- Price hikes to Ontario restaurant menus were cited as the driving factor in the 1.9% increase in January inflation

- Ontario business confidence ranked sixth among the 10 provinces in January according to CFIB at 58.7 – off 4.7 points from January 2017

- Ontario's year-over-year exports to the U.S. down for the sixth consecutive month

- Legend3D, a Los Angeles-based digital media company all but closed up shop. The government had given them $3.1 million, claiming 271 new jobs would be brought to Ontario

March – D-Day (Debt-Deficit)

The 2018 Budget was the big news this month, and I'll get into that after a quick look at what we learned throughout the rest of the month. It should come as no surprise that the government rolled out a series of pre-budget, pre-election announcements. Among them was a $105 million pledge to help Ontario's horse racing industry. This, from the same government that gutted the same program through cancellation of the Slots at Racetracks program in 2012. Court documents show the government was prepared for the "collapse" of the industry and forecast the loss of 23,000 jobs and deaths of 27,000 horses. A $65 million lawsuit from the industry is expected to proceed in court this spring. Nonetheless, the government shamelessly announced its re-birth.

Doubling down

The Fraser Institute shone the most illuminating light on the true state of Ontario's finances in a report entitled *Ontario's Lost Decade: 2007-2016*. It stated that Ontario was "mired in a prolonged period of economic weakness during which it lost ground compared to the rest of the country." Among the findings were that Ontario was dead-last among provinces in real median household income growth, second worst in new debt per capita, and third last in private sector job growth.

It should be no surprise that the Canadian Manufacturers and Exporters called for a "pro-growth manufacturing strategy for Ontario." They noted manufacturing sales growth in 2017 was less than 1%, the worst of any province, and Ontario's slow growth has helped Canada's ranking in global manufacturing output fall from 9th two decades ago to 14th. They also point out (contradicting the Finance Minister) that foreign direct investment into Ontario has shrunk by over 2%, compared to growth of 30% in the U.S. It should come as no surprise that Central1 reported that Ontario manufacturing decreased 2.3% in January.

The C.D. Howe Institute was even more blunt in its report *Fiscal Soundness and Economic Growth: An Economic Program for Ontario*. The very first sentence reads "Ontario is on an unsustainable fiscal course." It says the government must act to bring the long-term cost of government in line with the revenue-raising capacity of the province. It proposed 15 steps Ontario should take, not the least of which is "Restate the province's books to reflect the Auditor General's recommended accounting treatment of pension assets and electricity sector debt."

Finally, we already know that we have the largest subnational debt on the planet and that our debt is larger than 75% of the world's countries. But Ontario's crushing debt was put into perspective by the National Post's Tristan Hopper. What he pointed out is that it would take music superstar Drake 2,500 years to pay it off based on his earnings from last year! Hey … maybe putting it into a pop culture perspective will make people sit up and take notice! The $12.3 billion in interest Ontario pays on that debt is enough to send one million students to school, or as another writer put it, is enough to build a new ($1 billion) hospital EVERY MONTH. Since 2003, the current government has doubled spending from $71 million to $141 million and increased the debt from $139 billion to $312 billion.

Another electricity scandal?

We heard shocking testimony from the Auditor General this month regarding her audit of the Independent Electricity Sector Operator (IESO) as it pertains to the accounting methods used for the government's hydro plan. It seems this government has learned no lessons from the Gas Plant Scandal and cover-up. The Auditor has said she thinks "the accounting is bogus," and highlights the fact that the financial and accounting structure was designed to avoid reporting the unfair hydro scheme's costs. She claims it was "allowing the government to falsely claim" their budget numbers. The government's fiscal numbers can't be trusted.

The Auditor's concerns also included "incorrect accounting, deceptive and obstructive behaviour by the IESO's board and management, and poor financial controls." It's so bad, the Auditor General warned that if the improper accounting isn't fixed, she might issue an ***adverse*** opinion on Ontario's books. That would be a first in Canadian history for any government's financial statements!

The audit of IESO shows "the annual deficit would be understated by $1.3 billion" due to the government's highly questionable hydro plan accounting. But worse, the Auditor is being obstructed from doing her work by IESO officials. She says "they continually say they're co-operating, but they stalled on giving us information," and "wouldn't sign the management representation confirming that they gave us all the information."

The Auditor also reported IESO paid $600,000 to KPMG last year, nearly seven times its normal annual audit fee. She said "They say that we cost $230,000 to answer our questions. It's ridiculous." She also found that $1 million in security deposits were not reconciled because they couldn't figure out who the money was owed to!

Also, according to the Auditor, IESO held a board meeting to approve their statements but they didn't tell her or her staff. She said "My team kept saying, 'Well, when is the board meeting? We'd like to come.' They did it without telling us."

The AG learned that "the assets of IESO have been pledged as collateral and security against the fair hydro trust." She discovered that "in a box of papers after we were basically finished the audit and not given to us online like most of the other documents." What does that mean? According to the Auditor "it means is that the generators fall behind the creditors for the fair hydro plan trust." Is the government playing financial games with Local Distributor's assets?

The bottom line is the Auditor General has authority to audit the province's books. Yet this government has fought her time, and time again. They have attacked her credibility, they have attacked her expertise, and they have attacked her character. It has gone too far.

As a post-script to this hydro story, the month ended with Hydro One publishing their top five earners list (a requirement). President and CEO Mayo Schmidt has been doing such a wonderful job, that he received a $1.7 million raise last year. Yes, that's just his raise – not his salary. With shares and other compensation, his 2017 pay was $6.2 million.

Even the Premier can't deny it any longer

Messaging from the Premier's Office has grown ever more confusing and contradictory in the past month. In a pre-election announcement regarding prescription drugs, the Premier's release refers to "this period of economic change and uncertainty." This is a far cry from the 'everything is great' picture the Finance Minister crows about on a regular basis, highlighted by false boasts about leading the G7 in growth. The Premier can't have it both ways, so which is it?

The Premier also confirmed her cap-and-trade carbon scheme is nothing more than a government cash grab. She tweeted that eliminating her carbon pricing plan will "put as many as 40,000 public sector jobs at risk". As the Toronto Sun's Lorrie Goldstein noted, this proves the plan is not about reducing emissions, but instead, "its primary purpose is to retain government workers." Sohail Gandhi expanded upon this carbon revenue obsession in a Huffington Post column, stating bureaucratic impediments "are why innovative companies with technology that can fight climate change won't start up in Ontario."

Obsessed with revenue

The Financial Accountability Officer (FAO) provided a startling update on the amount of revenue the province is collecting in service fees in Ontario. The province forecasts that it will collect $2.9 billion in service fee revenue in 2017-18, an increase of 8% from the prior year, and a staggering 45% increase from just six years ago. The government added five new fees and increased 90 others in the last year alone! And most were increases above the rate of inflation. Vehicle and driver registration fees raked in $1.7 billion, or nearly two-thirds of the total.

Trading places?

Comparisons between Ontario and Quebec grew even less favourable for Ontario this month. BMO chief economist Douglas Porter noted Quebec already carries a higher credit rating than Ontario, prompting an old colleague of his to quip "What kind of bizarro world are we living in, where we in Toronto are looking up in admiration to Quebec on fiscal policy?" Meanwhile, Bloomberg reported Quebec's efforts to get its fiscal house in order are helping it achieve lower borrowing costs, and its bonds are outperforming those of its provincial peers. Average Quebec government bond yields narrowed 17 basis points in the past year to 55 basis points, while Ontario compressed by 14 points to 57 basis points. "Simply put, Quebec has been better behaved" said Franklin Bissett's Brian Calder, who added the uncertainty surrounding Ontario's deficit is likely to weigh on Ontario bonds. (More reaction in the April chapter).

Ontario's debt and deficit situation is only worsening under this government, threatening the broader economy, hurting families and hampering our competitiveness. This situation is made even worse by a revenue-obsessed government which refuses to properly report its finances to the officers of the Legislature and the public as a whole.

Other headlines

- Small business confidence in Ontario remains in the bottom half of all provinces in February.

- BMO Capital Markets data showed Ontario was the "only province that experienced a significant increase" in restaurant price inflation in the first two months of the year, following implementation of the minimum wage increase in January.

- Canada, China, and Hong Kong are among economies most at risk of a banking crisis according to the Bank of International Settlements due to high household borrowing levels.

- Toronto home sales in February were down 34.9% year over year, the 11th consecutive month of decline for year-over-year numbers.

- February stats show Ontario failed to recover all of the jobs lost in January after implementation of the minimum wage, seeing a net loss of about 35,000 since the start of the year. In the Legislature, the Finance Minister claimed Ontario has the lowest unemployment in Canada, which is false. BC has the lowest unemployment rate in Canada at 4.7%.

March – 2018 Budget

Hey big spender

The election document the government refers to as its 2018 Budget is proof this government will say anything, do anything, or promise anything to cling to power. Just months after promising balanced budgets for years to come, the government would plunge Ontario into six more years of deficits, just to announce a series of expensive election promises.

These promises are designed to fix the problems created by the government in the first place. Through cuts and inaction, the government created a crisis in mental health. Because of skyrocketing hydro, cap-and-trade, and increased fees and taxes, families are facing challenges with childcare and other costs. And seniors deserve the best health care possible, but weren't receiving it. They've had 15 years to address these problems, yet chose to show they 'care' only weeks before an election.

Personal tax increases

What the government failed to announce, but forms a major part of the budget, are $2 billion in new taxes on families and businesses, and skyrocketing debt that will further dilute the services families expect.

- In Ontario there are currently five personal income tax brackets and two surtax brackets charged once you eclipse a certain amount of annual income.

- The government is removing the two surtax brackets and instead creating seven tax brackets. This will raise taxes on an additional 1.8 million Ontarians by $200 each and decrease taxes by $130 for about 680,000 Ontarians.

- This is a personal income tax increase and will take $275 million out of families' pockets.

Business tax increases

The government is adding to the Employer Health Tax, impacting 20,000 businesses. Medium-sized businesses will each pay an additional $2,400 annually – that's $45 million in taxes. The government will also match the recent small business federal tax changes, including reducing tax exemptions on passive income. This change totals hundreds of millions in new taxes to small businesses. (More on this in the next chapter).

Altogether, the changes will increase taxes by a total of more than $2 billion over the next three years ($510 million this year, $715 million next year, and $780 million the following year).

The small print

One of the key budget admissions is found at the bottom of page 224. Only one time is it ever mentioned, but the word "efficiencies" is there in the small print. Yes, the government admits there are efficiencies to be found in the budget. In fact, there are apparently $1.425 billion worth of efficiencies, to be precise.

Annualized over the four-year term of the government, that first year of efficiencies alone equals $5.7 billion. When you find the same amount of efficiencies in the second year, and annualize that, you have a further $4.275 billion. Add in the third and fourth year, and that totals $14.4 billion in annualized efficiencies that the government is promising.

When we in the Official Opposition use the phrase "find efficiencies" the government screams "cuts". But these efficiencies, found in the government's own budget, were explained in the Legislature as finding "transformations" and finding "savings".

Economic concerns

Of real concern to Ontario businesses and families should be this government's dismal economic outlook. The budget projects $1 billion less in corporate revenues every year, due to "increased economic uncertainty" caused by the U.S. corporate tax cuts. It's ironic … the U.S. cuts taxes to make the States more competitive; our government's response is to raises taxes. Their answer is to run us into deep deficits, hike taxes, and make life more unaffordable for families. The government's own job projections in the budget are cut in half from 128,000 new jobs this year to only 60,000 jobs by 2021. You would have to ask … why is this government doing the absolute opposite of what's needed to create jobs in Ontario?

As CTV reported, "This budget had nothing for small businesses; those owners were looking for some kind of relief … in the 2018 budget they got nothing". The Coalition of Concerned Manufacturers rightly said: "true to form, the (government) did not support Ontario businesses in the budget … not acceptable, not right, not going to be tolerated".

Perhaps most damning is the comment from the government's own expert witness at the Pre-Budget hearings, Craig Alexander of the Conference Board of Canada. He said "There really isn't a rationale for running deficits" right now. Douglas Porter, chief economist at BMO also said "Ideally you would like to see government finances in relatively strong shape when we hit that heavy weather."

From the Auditor General

The Auditor General has pointed out three areas where the budget does not include costs that should be listed. While I covered these earlier in the book, it's safe to say they will add billions in debt and deficits.

- The IESO has not properly recorded assets and liabilities leading to $1.3 billion that is not recorded
- The government is counting outside unions' pension plan assets as their own, leading to an additional $860 million deficit this year
- The so-called Fair Hydro Plan is not on the government's books

We are looking to the Auditor General's Pre-Election Report to provide details of these three items, and more. Only then will we have a clearer picture of the state of Ontario's finances.

By the numbers

- The total government spend for the next year is $158.5 billion, up $9 billion from the year prior
- The deficit for this year will be $6.7 billion. The deficit will remain constant for three years then slowly return to budget balance in 2024-25 – 6 years from now. The government has not shown how. That means that they will have to either cut $6.7 billion worth of programs or raise taxes by $6.7 billion to reach balance
- The net debt will eclipse $325 billion this year
- Interest on the debt is $12.5 billion – more than $1 billion a month just to service the debt. Interest will rise to $13.8 billion by 2020-21; to $16.9 billion by 2024-25
- The net debt-to-GDP ratio increased from 37.1% to 37.6% as opposed to a planned decrease
- The 2017-18 budget year will end with a small surplus of $642 million, however it relies on $600 million from the contingency reserve to get it there

As this summary (from the National Post) illustrates, the government has made promises to nearly every voter demographic.

Seniors

- $575M to make drugs free for seniors
- $1B over three years, for a senior home care benefit (very similar to the program they cancelled in 2017 claiming the program had lower than projected take-up and provided little support to low-income seniors)
- $650M over three years for more home care
- $100M over three years for dementia strategy
- $300M over three years to hire new registered nurses in long-term care homes

Parents

- $2.2B over three years, providing some parents free child care (beginning in 2020)

Uninsured

- $800M over two years for drug and dental coverage for people without insurance (up to $700 for a family of four)

Disabled

- $2.1B over four years for mental health care
- $1.8B over three years to expand services for developmentally disabled

Unemployed

- $935M over three years on Good Jobs and Growth Plan
- $2.3B over three years, for 3% annual raise for those on Ontario Works or the Ontario Disability Support Program

Indigenous

- $40 million over three years to improve on-reserve child care
- $290M over six years in an effort to double child-care capacity on-reserve
- $1M to help provide healthy food to remote communities

Health

- $822 million (4.6%) increase in hospital funding this year

As I stated earlier, many of these promises were announced to address the problems created by this government, in the first place. And seeing as the promises were announced only weeks before the election, many stakeholders expressed scepticism that they would ever occur. The Toronto Star put it best in their editorial response: "These aren't announcements from a government with a clear path to turning them into reality." They also stated Minister's "promise-everything budget" runs the risk of "offering too much of a good thing at a moment when their credibility is stretched very thin."

When we received the *Bill 31 – Plan for Care and Opportunity Act (Budget Measures) 2018*, their concerns were quickly validated. None of the funding announcements outlined in the previous summary were even mentioned in the actual Bill. You would think that if the government was serious about implementing any of the promises they made to seniors, parents, disabled, and others – that they would get started immediately. There are barely 20 sitting days between budget day and the day the election writ drops. And many of those days will get eaten up debating Bill 31 – so there are very few days left to bring those promises into reality.

What made it into the Bill are all the tax increases – there was no wasting any time to put those into law! Not only the previously-mentioned $2 billion in taxes, but two additional items. Currently, there is a portion of the Taxpayer Protection Act of 1999 that prohibits the introduction of a Bill that increases a tax rate in a designated tax statute. This current Bill will exempt any Bill that receives First Reading in 2018. This will allow the government to bring further tax increases before the end of 2018.

Further, there is a new law that requires prescribed businesses "to record all sales transactions in an electronic cash register that meets prescribed requirements and to transmit the sales information to the Minister within the prescribed time, manner, and form." As if having to buy a $3,000 electronic cash register for your home hair or tailoring business isn't enough, if the government suspects you're not using the proper register, you can expect them to get a warrant and enter your home. Failure to comply brings you a $10,000 fine!

We also discovered one very interesting wording change. Schedule 3, which brings into law the very last sentence found on page 307 of the 307-page budget. It gives the government wide latitude to divert cap-and-trade revenues to projects "reasonably likely" to reduce greenhouse gases. That is quite a shift from the announcement of the justification for the government to implement the cap-and-trade tax. And deeper into the Bill, we realize that not only are they going to be able to fund just about any infrastructure project from cap-and-trade revenue, the government can now fund expenses incurred in 2015 – even before cap-and-trade was discussed, let alone made into law! It's timely to mention that over $3 billion in infrastructure went unspent last year, and more than $6 billion remains unspent over the last three years.

April – Post-budget reaction

The post-budget headlines instantly captured the sentiment across Ontario … "Spending taps open", "Brace yourself Ontario", "How much will all the freebies cost?", "Election free-for-all costs us all", "More spending, more fiscal problems, more debt", and "Too much for voters to swallow."

As is the custom, four hours after the budget is delivered, the Finance Minister and the Critics appear on TVO's 'The Agenda'. The Minister was filmed in his office, and I watched as he stated the government has "slayed the deficit" and "balanced the books", we're "projecting 140,000 (new) jobs every year", "we are the top in foreign direct investment" destination, and our "debt-to-GDP remains the same and will be tapering down". I was gobsmacked.

Not one of those statements is true. In fact the polar opposite would be closer to the truth. Let's go through them one-by-one.

- how can the deficit be "slayed" when the budget reveals deficits for the next 6 years?
- the books are artificially "balanced" by using 100% of the reserves
- the actual job creation numbers will not be "140,000 every year" – this year is 121,000 followed by 77,000 in 2019 and falling to 62,000 in 2020

- while we were once the number one foreign direct investment destination in North American, we have since fallen to 3rd
- Ontario's debt-to-GDP does not remain "the same" – it is in fact up by half a percent, from 37.1% to 37.6% and we are not "tapering down" – it is expected to rise to 38.2% in 2019-20 and to 38.6% the year after.

In the last chapter, I mentioned that none of the funding announcements outlined in the budget made it to the actual Bill. On TVO, when I was asked which of the budget gifts our Party would consider, I answered that the government never intended to deliver on any of them! I used the example of the Seniors' Healthy Home Program, one of the government's Top 10 Budget Highlights. It states it was designed for seniors "**to help them live independently**". Funny, in 2017 they just cancelled a similar Healthy Homes Tax Credit "**to help seniors live independently**" in their homes. Sound familiar? They cancel a program, and re-introduce it as one of their star programs in the next budget. And they cancelled it because it "had significantly lower take-up than projected" and "provides little support to lower-income seniors." Seriously, they must think we don't read! This is why I said that they didn't deliver a budget; they were reading an election document.

The Toronto Star seems to agree with me. Their Editorial was entitled *Ontario (government) ambitious budget may be too much for voters to swallow*. "So much at such a cost will strain the credulity of voters, who may well wonder why the (government) didn't do more during their 15 years in office." They go on to discuss the importance of many of the ambitious programs and deduce that "these aren't announcements from a government with a clear path to turning them into reality." At least I wasn't out there alone suggesting this. They conclude "With election day just over two months away, voters are bound to see them for what they are – $20.3 billion worth of promises from a government and party fighting desperately against the odds for re-election." Again, I'm pleased I'm not alone in my thinking!

The pile-on continued as RBC Economic Research prepared a sobering budget report entitled *Deficits by choice*. They conclude that a return to deficit is a matter of choice. The cumulative deficit over the coming three years totals $19.8 billion, approximately equal to the government's $20.3 billion in newly-announced initiatives. "What is worrying about this plan is … most of the measures are recurring entitlements. It makes the choice fraught with risk." While the government offers a return to budget balance (in seven years) "there are no details on how they will achieve it. This is concerning since so much spending kicks in late in the fiscal plan. Six more years of deficits may be optimistic." And like virtually all analysts, they end with "If Ontario is running large deficits when the economy is performing at capacity, what happens if a recession comes along? A pre-existing deficit and an elevated debt burden will limit the government's ability to respond and virtually guarantee a rapidly deteriorating fiscal situation."

Of more concern should be the warnings from the credit-rating and bond agencies. On budget day, both Moody's Investor Service and DBRS immediately issued warnings to the Ontario government over its plan to run deficits for the next several years. The two credit-rating agencies said the fiscal plan, which includes billions in new spending, would harm the province over the long term. Moody's led off with "The return to deficit spending is credit negative as it raises the likelihood that the province faces a structural deficit, in addition to increasing our forecast of the debt burden to accommodate the associated new borrowing." DBRS followed with "It demonstrates in the clearest term that the province is not committed to disciplined fiscal policy." While both agencies stopped short of downgrading Ontario on budget day, they shared that Ontario's creditworthiness could come under pressure as a consequence of returning to deficits.

Three weeks after the budget was delivered, Moody's delivered a message of their own. They changed their outlook on Ontario to negative from stable on Ontario's Aa2 ratings. The said it reflects their "expectations that spending pressure will challenge the province's ability to sustain balanced fiscal results across multiple years." Furthermore, Moody's "assumes that the financing requirements will be larger than previously assumed, leading to an upward trend in the debt burden and a faster rise in interest expense than previously anticipated." They concluded that "Financing to fund deficits and capital spending will continue to push the debt burden higher" and "Increased debt financing will also occur during a time of rising interest rates, which will accelerate the increase of the province's interest expense."

And as mentioned in an earlier chapter, a deficit would likely weigh-in on Ontario bonds, and that's exactly what occurred. When Ontario and Quebec offered up their bonds at the beginning of the month, Quebec came out on top, selling its securities at a spread 8 basis points closer to the federal benchmark than Ontario. Quebec sold $500 million of new 2.75% bonds at 65.5 basis points above federal government bonds, while Ontario sold $750 million of new 2.9% bonds at 73.5 basis points over the benchmark. All bonds have a similar maturity date. Why did Quebec win out? Well, they outlined their plan to deliver a balanced budget for five consecutive years, pay down debt, and lower taxes for small businesses. In contrast, Ontario will plunge us into six years of deficits, add billions in debt, and increase business taxes. Robert Kavcic at BMO sums it up with "Quebec has made meaningful progress on its fiscal situation, while Ontario has done little else but spend the recent economic windfall."

The cumulative effect of Ontario's record-high input costs caused the Ontario Chamber of Commerce to weigh-in. They have asked the government to rescind the small business tax increases included in the 2018 budget. "At a time when industry in Ontario is feeling the impact of the rising minimum wage, significant labour reforms, increasing global and U.S. competition, and rising input costs, we need government to reduce the cumulative burden, not add to it," said Rocco Rossi, President. The Chamber called on the government to remove the two proposed tax reforms that will cost employers nearly half a billion dollars in new taxes.

The government certainly doesn't acknowledge the fiscal imbalance it has created, nor do they understand the trouble it is causing in the marketplace. The early April numbers are out: exports decreased in February, small business confidence fell to 57.1 from 59, and Toronto home sales were down 39.5% compared with a year ago.

Other headlines

- Auto insurance rates increased by 2.2%; despite the government's 2013 promise to lower insurance rates by 15% by August 2105, insurance rates have only gone down by 3.2% in five years

- The Canadian Federation of Independent Business (CFIB) survey found near record-high confidence in Quebec, where firms are basking in the limelight of improved fiscal finances and tax relief, contrasting with sagging sentiment in Ontario
- BMO Capital Markets showed that business competitiveness took a hit when the U.S. government reduced taxes, erasing the large advantage for Canadian firms. As if to rub salt, domestic policies have increased business costs and red tape, with higher climate protection charges, minimum wage hikes, and new salary rules for part-time/casual workers in Ontario
- BMO also noted that private-sector investment in Ontario declined by 4%
- Central 1 said new housing starts declined 30.4% in March (-12.2% for Q4); the price of a new single-detached home declined as well, posting the highest month-over-month decline since last July
- Q4 Ontario Economic Accounts showed that Ontario is not "leading the G7 in growth" as the government likes to pronounce – growth was 0.6% vs 0.7% for the U.S.

GAS PLANT SCANDAL

GAS PLANT SCANDAL

Any conversation regarding finance wouldn't be complete without mentioning the government's Gas Plant Scandal, as this not only cost the taxpayers $1.1 billion, but shone a light onto the inner workings of this government.

After the 2011 election, 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, and we finally have a legal resolve to the second. It shouldn't have taken an OPP criminal investigation and the sound of jail doors slamming to get that answer.

You may find a little hyperbole and vitriol in these next pages. After all, as our Party's lead for most of the Gas Plant Scandal, I had a front-row seat. Beginning in the fall of 2012 and working through the winter and summer Legislative breaks and on into the spring of 2014, with daily meetings and twice-weekly televised Hearings, we faced an entrenched opposition. The former Premier mocking me didn't help. After I first announced in the Legislature that this would be another "billion-dollar scandal", the 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 government 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 government cancelled a contracted gas power plant in Oakville. Then in September, 2011, with the future Premier as co-chair of the government's re-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 government 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. The Premier herself has admitted the cancellations were "a political decision." As we now know, Ontarians are paying dearly for this latest 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 the Energy Minister 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 the minister 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 counteroffer 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 the future Premier 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 private arbitration where the proceedings and the results would be kept secret. In order to secure an agreement, the government waived valid defences and gave up the benefit of judicial limits on damages. They hid the majority of the settlement costs on the hydro bill, while only talking publicly about the much smaller taxpayer portion of the costs.

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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 government, and the government alone, decided to relocate the gas plants. The Mississauga plant is now built in Lambton, while the Oakville plant is near Napanee. Because they 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 government decision to move the Oakville plant so far away, 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 this government. In May, 2012, a former colleague and MPP from 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 36,000 documents, four months after the initial request. At that time, we were told we had all the gas plant documents. Two weeks later, shockingly we received another 20,000. We would later hear sworn testimony that an Energy Ministry staffer with long-held government ties, was sent to the Ontario Power Authority to instruct them to withhold certain documents. As we were assessing these new documents, the Premier shut down the Legislature and resigned three days later setting the stage for the current Premier to take over. In February 2013, even more documents came forward. Only now do we know that the February document-dump was after the computers in the Premier's office were wiped clean. Later, when we pushed, we received even more files. The total, according to the Premier, is now over 300,000 – that's 18 months after being told the original batch of 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 e-mails. We now had proof that there was indeed a cover-up, as we alleged from the day they tried to pawn of the 36,000 documents as 'all the files'. 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."

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

I called the Commissioner of the Ontario Provincial Police to report a crime – the theft of data belonging to the people of Ontario. My former colleague and I wrote to the OPP to file a criminal complaint. Throughout that next year, OPP investigators visited the current Premier's office, executed a search warrant at a data storage warehouse, executed a further search warrant, as well as a warrant to explore a senior government official's BlackBerry.

As a result of information obtained from the first warrant, the OPP alleged the former Chief of Staff to the Premier, David Livingston, 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 the boyfriend to delete the Gas Plant Scandal files. The government's Party repaid the $10,000 – an admission they did pay to destroy evidence.

Here is where you normally would read a disclaimer that states "None of these allegations have been proven in court." Except now – all has indeed been proven in court. The Chief of Staff to the former Premier has been convicted and sentenced to four months in jail (now under appeal).

But back in March 2014, the headlines read "Police Suspect Computers Wiped", "Police Probe Premier's Aide", and "Top Aide Suspected of Crime." It took four years from the date those headlines first told us what would eventually be proven to be true. Sitting through the years of Hearings, we always knew something was not right. We accused many people, all under oath, of not being forthright with the Committee. But we were unaware that we were up against a massive cover-up being orchestrated by government insiders. Now we know there was a systemic pattern of deceit operated from the highest levels of the government. They did absolutely everything to thwart us at every opportunity, but we persevered. The trial provided many 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. Sadly, no judgement will return the $1.1 billion to the people of Ontario.

Today, the headlines read "Guilty". The Judge's 'Reasons for Sentence' is a remarkable read. Some of the highlights:

Mr. Livingston deceived the Secretary of Cabinet; … true plan was to eliminate sensitive and confidential work-related data; … attempted to destroy data on the hard drives of colleagues; … all at the time FOI requests in relation to gas plant documents were outstanding.

The defendant deliberately directed the deletion of e-mails and wiping of OPO computer hard drives to ensure that records relating to the gas plant controversy were destroyed Mr. Livingston attempted to interfere with the proper functioning of parliamentary democracy; … engaged in sophisticated and careful planning to eliminate work records This offence is very serious because it involves an attempt by the defendant to thwart the core values of accountability and transparency that are essential to the proper functioning of democracy; … strikes at the heart of the democratic process; … an afront to and an attack upon democratic institutions and values, …The defendant's conduct was egregious; …committed this offence because of political expediency, rather than fulfilling his responsibility to conduct himself within the law.

The most sobering lesson of the gas plant scandal may be this – if the government had won just one more seat in the 2011 election, none of this would have ever come to light. They would have retained their majority. Any attempt at Committee to get documents would have been voted down by the majority government; the Gas Plant Scandal hearings would never have happened. The government tried to stall, delay, and thwart us at every turn in our bid to get to the truth. They have consistently put their own interests, and the interests of their Party, ahead of the people of Ontario.

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 Lysyk 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.

THE STATE OF ONTARIO'S FINANCES

THE STATE OF ONTARIO'S FINANCES

To get a real picture of where we are today, let's look back at the opening and closing chapters of the last four *Focus* books. It's amazing how you could almost drop those paragraphs into this year's book, and they would still be relevant. It's actually quite disturbing to see just how little has changed in five years.

The original *Focus on Finance* opened with a tale of Ontario having the highest energy rates in North America, highest payroll taxes in Canada, crushing red tape, and listing several high-profile companies who announced they're leaving the province. It pointed out that Ontario, once the economic engine of Confederation, had become a 'have-not' province, relying on equalization payments from the federal government. And it reminded us that before this government took office, Ontario boasted a low debt-to-GDP ratio, low unemployment, cheap hydro, and reduced red tape. Wow ... literally nothing has changed – I could use the same paragraph from 2013-14.

The book described the ideological decisions that were made by the government, and the resulting consequences. Considerable evidence was provided that the finances in Ontario were far worse off than the government had disclosed. Remember, this was during the Gas Plant Scandal, where the government was forced to turn over once-confidential financial records – documents they never dreamed anyone would ever see. They illustrated there was no clear path to balance, considering the government had started a spending spree under the guise of recessionary stimulus funding. It ended with a stark warning brought on by the government's refusal to provide financial reports mandated under the Fiscal Transparency and Accountability Act. I concluded "The government is hiding the truth, because any of these reports would demonstrate the province is not on track to balancing the budget by 2017-18. The government continues 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."

Focus on Finance 2 opened up with quotes from a number of respected groups, all ringing alarm bells about Ontario's finances. 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". The title of the Ontario Chamber of Commerce report on Ontario's debt and deficit was *How Bad Is It?* As if the title wasn't enough, 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% 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".

The pages of the book painted a clear picture of the problems affecting families and businesses. Hydro was a significant focus, yet was still not on the government's radar. Higher taxes, especially through service fees, was a growing concern. And red tape was increasingly becoming a barrier to businesses looking to locate or expand in Ontario. Clear evidence was presented that because the government knew they had no path to balance the budget by 2017-18, they hatched a plan to artificially achieve that goal. They would begin to sell assets and put the funds directly into each years' revenue. John Ivison said it best in his National Post column when he wrote, "The province's finance minister had fluffed the books for this year and next, with net revenue gains from 'asset optimization' totaling $2 billion."

In Focus on Finance 3, the breadth and depth of the government's plan to use onetime revenue to artificially balance the budget by 2017-18 was detailed. It illustrated the difference between the 2014 budget, where very little 'Asset Optimization' was required for transit and infrastructure, and the 2015 budget, where suddenly the proceeds from the sale of Hydro One were now listed as part of operating revenue. And it disclosed, for the first time, the fine-print of the budget Bill where one sentence buried in the end of the book gave the government the tools it needed to artificially balance the budget – it allowed them to reimburse themselves for money they already spent on infrastructure.

The book concluded that there's a cumulative affect that's hurting Ontario. It's not necessarily one decision or another – it's the piling on of these decisions. Whether it's the increasing regulatory burden, skyrocketing hydro rates, or future cost increases from cap-and-trade – add them together and they are the reasons why businesses continue to flee Ontario, or choose not to locate here. Ontario has become the weakling and other jurisdictions are poaching us.

Last year's book began the same way as this year – by outlining a disturbing trend playing out with so many government ministers. They say one thing in the Legislature, in news conferences, and in government releases, when in many cases, the polar opposite was true. This is also what happened with the hydro file, where the public was told one story, but the experts and Legislative Officers revealed a more nefarious version. The book provided definitive proof that the government finally understood people believed their electricity rates were too high, that this was hurting our economy, and that the government's poor decisions and poor management were responsible. Then they blamed the increases on issues they knew people approved of, even though they were not the cause of the increases. And they concocted a plan using financial engineering to bring temporary relief; a plan proven to be more expensive in the future. Instead of fixing the core problem at hydro and stop signing more contracts for power we don't need, they chose to kick that can down the road. They're adding a minimum of $45 billion in financing costs to artificially lower hydro bills – money that when paid back will cause those bills to soar, even more.

Focus on Finance 4 ended with a just-released Financial Accountability Office News Release stating "FAO Expects Steady Deterioration of Ontario's Budget Deficit Without Additional Government Measures." The FAO delivered an explosive report confirming Ontario's budget is not in balance, and we can expect "continued budget deficits over the next five years, reaching $6.5 billion by 2021-22." While the government declared a balanced budget for 2017-18, the FAO projects a deficit. They describe the scenario where the government is using "$3 billion in one-time revenues." They also describe higher revenues came from "strong growth in tax revenues (housing) and a boost from onetime, non-tax revenues (sale of Hydro One, OPG building, etc.)." Beginning next year, the growth in tax revenues is projected to be moderate, while the boost from onetime, non-tax revenues will end.

What's alarming is that so little has changed over the last five years. While the government has declared they have balanced the budget, the use of one-time revenue sources masks the seriousness of the situation they have created.

Clearly, the message is not sinking in. Years of waste, mismanagement, and scandals, have not had any affect on the government's thinking. They continue to kick the fiscal can down the road, hoping that revenue growth will eventually catch up to their spending. But they can't help themselves and continue to spend ever-increasing amounts of taxpayers' money.

MY
FINAL
THOUGHTS

MY FINAL THOUGHTS

There have been a lot of numbers presented over the last 124 pages. My final thoughts will sum-up what we've learned so far, drill down deeper, and present what the experts have told us is the real state of Ontario's finances.

The FAO

If we tally everything we've learned over the last 12 months from the Financial Accountability Office (FAO) and the Auditor General (AG), we come to a vastly different set of numbers than those provided by the government. In the 2017 budget, the government forecast reaching balance by 2017-18, to be followed by consecutive years of growing surpluses. The government shifted significantly in the 2018 budget; claiming to have balanced, but forecasting a return to deficits for the next six years. However, neither budget took into account the analyses and forecasts of the FAO, nor the explicit instructions from the AG.

Even with the government's lofty 'growing surpluses' promise in the 2017 budget, the FAO responded by forecasting deficits beginning in 2018-19. This is due to "the absence of one-time, non-tax revenues and higher program expenses." In their later fall economic report, they revised downward adding, "This is a significant deterioration since the FAO's spring outlook." They re-emphasized there will be loss of the one-time revenues and moderate tax revenue growth, resulting in a return to deficit in 2018-19. Of more concern is their forecast of a steady deterioration in the budget deficit over the outlook, reaching $3.6 billion by 2021-22.

They end their report with "the government has not adopted the Auditor General's recommended accounting framework, reducing the transparency and reliability of Ontario's fiscal projections." They are referring to the ongoing disagreement between the government and the Auditor General over the appropriate accounting treatment for the government's jointly sponsored pension plans, and the AG's claim that the government is not correctly accounting for the full cost of the Fair Hydro Plan.

The AG

In the fall of 2017, the Auditor General of Ontario issued a qualified audit opinion on the Consolidated Financial Statements of the Province of Ontario, saying the statements significantly understated the 2016-17 deficit, as well as the Province's net debt. The Government recorded the surplus for two pension funds it co-sponsors (Ontario Teachers' Pension Plan; Ontario Public Service Employees' Union Pension Plan) as a net pension asset. According to the AG, the deficit is understated by $1.44 billion for 2016-17 and the net debt is understated by $12.43 billion for 2016-17. In addition, the AG said the government inappropriately recorded the transactions between power generators and power distributors of the Independent Electricity System Operator. As a result, other assets and other liabilities in the consolidated financial statements are both overstated by $1.65 billion in 2016-17.

With respect to the Fair Hydro Plan (FHP), the Auditor General created a Special Report. In it the AG says the government created an unnecessary, complex financing structure to keep the true financial impact of most of its 25% electricity-rate reduction off the Province's books. "The accounting proposed by the government is wrong and if used would make the province's budgets and future consolidated financial statements unreliable," said AG Bonnie Lysyk. She estimates the total cost of the scheme to be $39.4 billion over 30 years, including about $4 billion in extra interest charges.

How that all adds up

If you take the government's numbers and include the accounting regulations of the Auditor General, which removes the pension funds and adds in the cost of the FHP, the government's budget deficit figure is off by at least $5-6 billion over each of the next four years.

If you include those same accounting regulation calculations, and add in the forecast budget (deficit) estimates of the Financial Accountability Office, the government's stated budget deficit figure is off by an additional $2-4 billion over each of the next four years! We will get a clear picture when the Auditor General's review of the pre-election finance report is released (likely while this book is at the printers).

Under either scenario (and we can be certain both the FAO and the AG will update their numbers now that the budget has been released), they are a far cry from the numbers presented by the government of Ontario. And that's the final point to be made. The government's numbers simply can't be trusted. Recall the words I underlined early in the book. Secrecy. Deterioration. Dangerous precedent. Unlikely assumptions. Significantly understated. Inappropriately. Hide. Unreliable. Conceal. Distort. Falsely. Deceptive. Obstructive behaviour. Bogus. Those were all words used to describe the government's accounting. Printed for all to read; published in reports by the Independent Officers of the Ontario Legislature, our Auditor General and Financial Accountability Office. Again, this should leave you with no doubt that the government's numbers simply can't be trusted.

If you would like to download previous monthly editions of the *Fedeli Focus on Finance* newsletters, or the three previous *Focus on Finance* books, go to **www.Fedeli.com** and click on the *Focus on Finance* link under *Media*.

A little bit about Victor Fedeli ...

Victor Fedeli is a life-long entrepreneur, specializing in communications. He opened his first company in 1978 and grew the firm into a wildly-successful full-service marketing company. In 1989, his Fedeli Corporation was named **34th in the 50 Best Places to Work in Canada!**

In 2003, Vic successfully ran for Mayor of the City of North Bay and served two terms. Few people get an opportunity to re-shape a City, and Vic took great advantage of his opportunity while Mayor. Simply put, he and his strong team of Councillors restored hope and restored solvency.

In 2011 Vic was elected as MPP for Nipissing. He was named Official Opposition Energy Critic, eventually heading up the Gas Plant Scandal Hearings. His shocking revelations – through once-confidential internal government documents – were critical in bringing justice to the people of Ontario for the waste of $1.1 billion in the politically-motivated cancellation of two gas plant projects.

After two years in Energy, Vic was named Finance Critic. In this role, he began publishing ***Fedeli Focus on Finance***, a monthly series of newsletters offering an in-depth look into the finances of Ontario. This led to the publication of the ***Focus on Finance*** book series – and this 5th volume.

Early in 2018, Vic's Caucus colleagues elected him as Interim Leader of the Official Opposition.

Victor Fedeli,
Nipissing MPP
and
Interim Leader
of the Official Opposition

April 2018