BUDGET ENVELOPES, POLICY MAKING AND ACCOUNTABILITY

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1. INTRODUCTION

This study reviews the evolution of the Canadian public budgeting system from the perspective of its relevance to the achievement of efficiency and effectiveness in an environment increasingly characterized by globalization and competitiveness. It appraises the effects of recent budgetary reforms on the achievement of greater effectiveness in the financial management system. The various reforms implemented have been less effective than anticipated which suggests that there are inherent institutional forces influencing the performance of the system. At least one analyst has pointed to the failure of several reform proposals under the general label, "the politics of public spending in Canada".[1] The changes which have occurred in the international and domestic environments have made the challenge of expenditure management more demanding. The political economy of globalism, competitiveness and deficit reduction has introduced new challenges which have led to proposals for further reforms.[2] We need to review the expenditure management system to make sure it is up to the challenges of the 1990's and beyond.

In the past, several of the reform proposals were influenced by domestic forces. However, by the 1970's, external forces were, once again, playing a major role in financial management reforms. For example, the expenditure reductions announced in 1978 by Prime Minister Trudeau were influenced by external forces. Again the reductions announced in the early 1990's have been influenced by external forces. Consequently, international environmental forces will probably continue to be important in influencing budgetary reforms. The persistence of the deficit since 1975 has been a major force driving further reforms to the financial management system.

There have been several initiatives within the past thirty years that were designed to improve the budgeting system in Canada. They represented a variety of responses to the internal political economy, but, as indicated above, some of the episodes were also largely influenced by external forces. For instance, the 1972 oil price shock led to major structural change in the western industrialized economies. The action profoundly affected fiscal federalism in Canada, among other things. In 1977, the Government of Canada introduced major fiscal changes with the passage of the Established Programs Financing Act. In fact, the expenditure management system was most significantly changed since 1975 which suggests that the period between the mid-1970's and the 1990's can be regarded as one of persistent reforms. On the whole, the reforms between the 1960's and the 1990's were adopted in response to domestic rather than to international forces. Consequently, the internal forces must be distinguished from the international ones because they affect the seriousness and the persistence of the reforms. Our review suggests that the most significant reforms can be related to the institutional shifts which have been influenced by both globalism and competitiveness. The adaptive nature of the Canadian expenditure management system stands out.

Important landmarks in the development of the Expenditure Management System considered in this paper are:

1) the Glassco Commission on the Organization of the Government of Canada;
2) the Lambert Commission on Financial Management and Accountability;
3) the Policy and Expenditure Management System;
4) the Nielsen Task Force which reviewed governmental programs;
5) the major changes in public accounting;
6) the reforms to the estimates and their implications for accountability and efficiency, including their submission to Parliament as Parts I, II and III;
7) the establishment of the Office of the Comptroller General and the implications of regular program evaluation for government efficiency;
8) the review of the federal Auditor General on the results of expenditure planning.
9) the establishment of the Expenditure Review Committee in the late 1980's which represented a centralization of the system from the perspective of the role of Cabinet Committees;
10) the system of expenditure management in operation in the early 1990's;
12) the introduction of Increased Ministerial Authority and Accountability (IMAA) by the Treasury Board; and
12) the establishment of a Task Force on Resource Management and Budget Controls within the PS2000 Task Force which made further recommendations designed to improve the resource management system.

Over the past thirty years, there have been a number of important initiatives taken to improve the financial management system of the Government of Canada that clearly illustrate the adaptive nature of the system.[3] A number of issues have emerged from the various reform initiatives. They include, among others: the relative emphasis which should be placed on centralization versus decentralization procedures; the significance of the Glassco Commission recommendations for improved expenditure management and the extent to which they were implemented; the relative roles of the Prime Minister, Minister of Finance and the President of the Treasury Board in expenditure management; the roles of the key central agencies - Finance, Treasury Board and the Privy Council Office - in expenditure management; the significance of the reorganization of the cabinet committee system for improved expenditure management; the relative emphasis which should be placed on political management versus financial management roles in the improvement of the expenditure system; the significance of the fiscal planning process in expenditure management; the relevance and importance of the fundamental flaws identified by the Lambert Commission report for improved expenditure management; the extent to which the Lambert Commission recommendations have influenced the subsequent reforms of the system;[4] the appropriateness and limitations of the Policy and Expenditure Management System introduced in the early 1980's which was characterized as envelope budgeting; the extent to which the Nielsen Task Force recommendations for improved management were implemented;[5] the effectiveness and limitations of the Expenditure Review Committee introduced in the late 1980's to control spending; the significance of the introduction of

Increased Ministerial Authority and Accountability (IMAA) for expenditure management; the importance of the New Management Initiatives introduced in the early 1990's; the rationale for and the significance of the introduction of operating budgets; and finally, the implication of increased globalization and competitiveness for reform of the expenditure management system and process. The various issues identified above may be captured within three broad reform periods between the 1960's and the 1990's. During the period from the 1960's to the 1990's, the expenditure management system evolved from a simple to a complex one and back to a less complex one within three stages.

First, there was the impact of the Royal Commission on Government Organization (Glassco) which emphasized greater reliance on management principles. Second, there was the influence of the Lambert Commission on Financial Management and Accountability which emphasized the need for improved role specialization among participants and improved accountability to parliament. Third, there was the shift in emphasis which occurred with the release of Agenda for Economic Renewal in 1984 which led to the subsequent formulation of the expenditure control plan. The persistence of the centralization/decentralization issue in the reform of the expenditure management system cannot be overemphasized given the fact that it emerged with the Glassco Commission recommendations of the early 1960's and has persisted to the early 1990's with the report of the Task Force Public Service 2000.[6] These issues are all discussed in this study. Together, they identify important elements in the politics of expenditure management.

It must be emphasized that the institutional reforms to Canadian public budgeting have been affected by a multiplicity of forces including; personalities, changes in management philosophies, competition between the department and other agencies involved in the process such as the Department of Finance, the Treasury Board Secretariat, the Privy Council Office, the significance and performance of the cabinet committees and to a variety of studies and recommendations by royal commissions and task forces including Glassco, Lambert, D'Avignon and PS 2000, to name a few. The system has been under constant reform. A number of valuational and structural changes have been present in the evolution of the system. They demonstrate a number of competing principles and issues such as political versus managerial decision-making and control, simple versus complex structural arrangements in the design of the budgeting system, comprehensive versus incremental reforms of budgeting, the extent to which the system should be controlled by spenders versus guardians and the highly complicated problem of ministerial responsibility and accountability, especially as it relates to the role of parliament and parliamentary committees in controlling the system of financial management. Given the length of the study, some of these issues are dealt with only in an implicit rather than in an explicit way. Overall, they point to the complexity of the public budgeting system and the necessity to examine institutional reforms in the new global environment of the 1990's.

Public budgeting systems have been affected also by management principles such as management by objectives, planning, programming and budgeting systems and zero based budgeting philosophies. While these systems were never fully implemented, they have functioned as guiding principles which have influenced periodic reforms between the 1960's and the 1990's. Each institutional reform has been consistent with a particular environmental context which supported the implementation of a particular system of budgeting. The centralization-decentralization debate can serve as an illustrative example of the ever changing structure and processes of public budgeting.

Most recently, Public Service 2000: The Renewal of the Public Service of Canada has indicated that the system requires a significant amount of decentralization of responsibility to managers who can be held accountable for their decisions. The Report of the Task Force on Resource Management and Budget Controls concluded that:

> the evolution of the current resource management system in the Public Service has been influenced not only by the changing needs of Parliament and Public Service managers themselves but also by a series of external

> reviews carried out over the years. Although one of those reviews did lead to more central controls, the major findings has been that the current range of government programs and initiatives can be most effectively managed and delivered if unnecessary central control is eliminated, and managers are provided with an adequate level of authority. It has also been consistently noted that such a system can function effectively only if there is a reasonable system through which managers can be held responsible for their decisions and for the exercise of their authority.[7]

Consistent with the above observation, the PS 2000 Task Force recommended the following changes in the financial management system. First, it recommended the abolition of the concept of person years as a measure of human resource needs. Second, it recommended the utilization of the concept of the operating budget. As a result, a number of institutional reforms are proposed for the 1990's; demonstrating, once again, the persistence of reforms.

This study reviews the experience of expenditure management in Canada from the point of view of its ability to affect the efficiency and effectiveness of government and its impact on the competitiveness of the private sector. In this regard, the study refers to some of the management initiatives adopted in response to the recommendations of the Nielsen Task Force. The Nielsen Task Force represented an attempt by the Government of Canada to incorporate the views of the private sector with respect to the need to improve the public budgeting system. The signing of the free trade deal with the United States, the initiative taken to extend the relationship to encompass Mexico, and the adjustments to the international trading system in general requires that the federal public sector be run in a more efficient manner and not constitute an undue burden on the ability of the private sector to compete globally. Accordingly, the study considers the extent to which the federal government expenditure management system has responded to international versus domestic forces. In addition, the study captures changes in the philosophy of governments; for example, changes in the ideological orientation of the Liberal and Conservative parties.

The shift from the Policy and Expenditure Management System (PEMS) in 1981 to the introduction of the Expenditure Review Committee in the late 1980's and its ultimate demise raises the issue of the relative roles of ministers and cabinet committees in the expenditure review process. The 1989 change suggests that the Prime Minister must be a key player in the process if expenditure restraint is to be successful. However, the emergence of IMAA suggests that the Treasury Board and the various departments are also important actors in the implementation of these strategies.[8] These issues raise questions concerning the extent to which there has been a shared culture of budgetary reforms in Canada between the 1960's and the 1980's. In order for the reforms to be effective they must permeate the overall decision-making system.

The evolution of the expenditure management system reveals the influence of political and economic factors, both of which need to be carefully examined. Political management of expenditures has been a central concern of Prime Ministers and ministers in ensuring that political priorities can be met. The changes in the cabinet committees between the 1960's and the 1990's demonstrate the extent to which various prime ministers have adapted the system to external demands.[9] For example, The composition of the 1989 Cabinet Committee System clearly indicated the challenges of globalization, competitiveness and financial restraint. In retrospect, the changes in the cabinet committee system have reflected shifts in priorities. The cabinet committee system in the early 1960's was the product of a period in which expenditures were significantly increased. The commitment in the early 1960's to expand social expenditures in the health, education and social policy fields introduced programs with major down-stream effects which were not constrained until in the 1970's. In the late 1960's, the Cabinet Committee on Priorities and Planning was established to formulate political priorities. It represented a concern with political priorities, an issue later criticized by the Lambert Commission. The Cabinet Committee on Social Policy represented the largest resource allocation in the Government of Canada's overall system. Consequently, by the late 1970's, steps were taken to shift resources from the social policy area. The introduction of the envelope system reflected such a change. The attached envelope shares of the expenditure plan between 1979-1989 shown in Table 1 clearly demonstrates this trend.

TABLE 1
Envelope Shares of the Expenditure Plan

(Percentage)	1979-1980	1980-1981	1981-1982	1982-1983	1983-1984	1984-1985	1985-1986	1986-1987	1987-1988	1988-1989
Economic & Regional Dev.	13.2	14.1	13.1	13.1	12.5	13.6	10.6	10.1	11.3	10.3
Social Dev.	49.1	48.1	45.1	47.8	48.3	46.3	46.6	46.7	45.5	45.5
Fiscal Arrangements	6.5	6.3	6.3	6.3	6.2	5.5	5.3	5.4	5.3	5.4
External Affairs & Aid	2.6	2.3	2.4	2.3	2.5	2.4	2.2	2.5	2.7	2.7
Defence	8.2	8.1	8.0	7.8	8.1	8.0	8.2	8.6	8.4	8.5
Parliament	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Services to Government	4.4	3.7	4.6	3.3	3.6	3.5	4.0	3.4	3.3	3.0
Total Program Expenditures	84.1	82.9	79.8	80.9	81.3	79.4	77.1	77.1	76.6	75.4
Public Debt	15.9	17.1	20.2	19.1	18.7	20.6	22.9	22.9	23.4	24.6
Total Envelopes	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Treasury Board of Canada, Expenditure Plan, Part I, 1988-89, p.17.

The Mulroney cabinet committee system introduced in the late 1980's represented a response to a most significant shift in the international and domestic environment. To understand these developments fully, it is necessary to examine the changing structure and process of the expenditure management system in Canada as it has evolved between the 1960's and the 1990's. The structure and process of expenditure management in Canada reveal a number of institutional changes. First, it evolved from a very simple system with a few actors performing several key roles to a complex one with competing and overlapping roles and responsibilities. Second, the roles performed by key players became more highly differentiated as the system evolved. The transition from the old to the new system was reflected in the Glassco Commission reform proposals and in the initiatives taken by the Bureau of Government Organization in implementing the recommendations.[10] The next two sections of this paper examine the evolution of the expenditure management system between the 1960's and the 1980's.

2. THE EVOLUTION OF THE EXPENDITURE MANAGEMENT SYSTEM AFTER GLASSCO FROM THE 1960'S

2.1 The Glassco Commission and the Reform of the Financial Management System in Canada

The budgeting system of the 1960's reflected a shift from one of extensive control one introduced in the 1930's to a focus on program budgeting recommended by the Glassco Commission. The reform led to the endorsement of a planning emphasis partially reflected in the structures of the Privy Council Office and the Treasury Board.

Since the 1960's, there has been a persistent problem with respect to the need to reconcile the conflicts between the central agencies with respect to financial and personnel management. Consequently, the Canadian system of financial management has displayed continuing conflict between centralization and decentralization. Timothy Plumptre has criticized the central agencies for being too involved in control rather than policy planning. The Glassco Commission recommended the centralization of the formulation of priorities by the central agencies, the Privy Council Office, the Department of Finance, and the Treasury Board Secretariat. It simultaneously recommended the decentralization of responsibilities to managers within departments.[11] The Commission also recommended program budgeting and in 1969 the Treasury Board issued a Program Guide within which departments would formulate their expenditure estimates. The reform proposals encompassed two competing principles in the design of budgeting.

The trends toward both centralization and decentralization were thus evident in the work of the Glassco Royal Commission on the Organization of the Government of Canada. The extent to which the system has shifted between centralization and decentralization must be critically assessed in that the reforms illustrate the complex relationships which can develop between the Prime Minister, the cabinet, cabinet committees, ministers and departments in the formulation of expenditure decisions.

The system of expenditure management in Canada has been significantly overhauled in response to a number of studies, some of which have involved input from the private sector. The Glassco Royal Commission on the Organization of the Government of Canada marked a turning point in the system when it called for sweeping changes in the central management function. It recommended the establishment of the Treasury Board Secretariat as a separate department concerned with personnel and expenditure management issues. The Report recommended the designation of more specialized roles for the Privy Council Office, the Treasury Board Secretariat and the Department of Finance. The Commission recommended the decentralization of responsibility to departments. The Glassco Commission outlined a management system for the Government of Canada encompassing the Prime Minister and Cabinet, the Privy Council Office, the Treasury Board Secretariat and the Department of Finance as key actors in the process. Since the 1960's, the system has experienced increased role specialization by the key central agencies. In the early 1960's, the financial management system was very simple. The key actors within the system operated around the Privy Council Office and the Department of Finance. The Minister of Finance performed the pivotal roles in the process. The Glassco Commission outlined a management system which encompassed at least three critical actors displayed in Chart 1.

CHART 1

General Plan of Central Authority

2.2 The Department of Finance: The Influence of Glassco and the Emergence of Strong Central Agencies

The 1964 Organization Chart for the Department of Finance (Chart 2) cited, reflects the transitional period during which the recommendations of the Glassco Commission were being implemented. It shows the Minister of Finance, the Hon. Walter L. Gordon, as Receiver General and Chairman of the Treasury Board. However, by then the Government of Canada had accepted the Glassco Commission recommendations, and the Prime Minister had assigned a separate Minister as President of the Privy Council and Acting Chairman of the Treasury Board.[12] A Bureau of Government Organization was established to effect the transition from the system which had existed prior to Glassco.

It is most important to note that the Department of Finance was, at this time, under the Deputy Ministerial leadership of R. B. Bryce one of those who had been attracted into government service during the 1930's by Clifford Clark, the Deputy Minister of Finance at the time. Moreover, R. B. Bryce had been one of the early Keynesian who was in charge of the economics division established within the Department of Finance in 1946. R. B. Bryce was such an outstanding scholar and economic analyst that he virtually dominated the department. Under his leadership, the Department thrived. However, the Department came in for some heavy criticism during the Walter Gordon ministerial leadership when outsiders were used to formulate his first budget in 1963. An alleged breech of the Canadian tradition of budget secrecy became a controversial public issue. Since that time there has been a continuing debate concerning the need to open-up the budgetary process. It continued to be an issue into the late 1980's and into the 1990's.

In 1964, the Department of Finance operated within a loose informal structure that represented the particular interests of the respective Assistant Deputy Ministers: A. F. W. Plumptre, International Programmes; A. B. Hockin, Economic Analysis and Government Finance and Guaranteed Loans; J. F. Grandy, Tariffs, International Economic Relationships and Resources and Development; and A. W. Johnson Federal-Provincial Relationships, Tax Policy and Social Security and Pensions. Strong Deputy Ministerial leadership, combined with collegial relationships, was a central feature of the department during the 1960's.[13] The 1960's were characterized by dramatic changes in the decision-making process in general and budgeting in particular. The period between the 1960's and the 1980's displayed a high degree of leadership turnover at Finance which was not altered until the Conservatives came to power in the mid-1980's. Financial management decisions were made in a department characterized by strong personalities, by highly collegial relationships, but with political interference and a high turnover in leadership. R.B. Bryce himself indicated later that there were six Deputy Ministers of Finance between 1867 and 1963 and six between the mid-1960's and the mid-1980's. His comments indicate the high turnover of senior officials between the 1960's and the 1980's. There were three Deputy Ministers of Finance between 1932 and 1968. Budget reforms occurred under the deputy ministerial leadership of Simon Reisman, Thomas Shoyama, William C. Hood, Grant Reuber, Ian Stewart and Marshall (Mickey) Cohen who served in the position after Bryce. A major reorganization of the department was carried out in 1984 under Marshall Cohen's leadership. The reorganization of Finance reflected the attempt to respond to changing international and domestic forces. Notwithstanding the reorganization of Finance, there was still a need to clarify the roles of the central agencies and this issue continued into the 1980's.

The changing role of ministers and selected departments is also important in the evolution of the expenditure management system. The role of the Minister and the Department of Finance is especially important in any examination of the expenditure management system. The status and importance of the Department of Finance has fluctuated enormously between the 1960's and the 1990's and it is an issue of major importance in the reform of public budgeting. Between the 1960's and the 1970's there was an intensive debate concerning the relative roles which should be performed by the Prime Minister's Office, the Privy Council Office and the Treasury Board Secretariat in financial management. The various changes in the role and status of the department are indicative of the effectiveness of the expenditure management process. The control of public expenditures in Canada has varied with the relative power and influence of the Minister and the Department of Finance in the expenditure management system. The changes represented important indicators of the reform of the public budgeting system and were emphasized in the recommendations of the Lambert Commission which reported in 1979. Several of the Lambert Commission recommendations were directed at elevating the role and status of the Minister and the Department of Finance. Let's review the manner in which the relationship between the key players in the budgetary process evolved between the 1960's and the 1980's.

2.3 The Effects of the Legislative and Administrative Reforms of the 1960's

The efforts to strengthen the role of the Department of Finance during the 1960's was partially offset by the strengthening of the Privy Council Office. In the early years of the Pearson Government, a Special Planning Secretariat was established in the Privy Council Office concerned with issues of human resources management which led to major increases in public expenditures. Between 1963 and 1970 a cabinet committee system evolved which played an important role in political management. In addition, a number of new departments were subsequently created.[14] The amendment to the Financial Administration Act in 1967 established a separate Department to support the Treasury Board. Under the provision of the Financial Administration Act, the Department of Finance is responsible for "the management of the Consolidated Revenue Fund and the supervision, control and direction of all matters relating to the financial affairs of Canada not by law assigned to the Treasury Board or to any other minister". It is through this mandate that the Department supports the minister in his responsibility for the country's economic and financial affairs.

Pursuant to these reforms, the Treasury Board was expected to be a key actor in expenditure management.[15] With the designation of a program branch Glassco had outlined a framework for program budgeting which was subsequently effected in 1969. Since then, the Program Branch has been a key player in the financial management system. Consequently, a more detailed study of budgeting would focus on the role of the Program Branch in expenditure management.

The system of financial management which had existed prior to the Glassco Commission recommendation is displayed in the Organization Chart for the Department of Finance in 1964 (Chart 2) which shows the Minister of Finance in his capacity as Receiver General and Chairman of the Treasury Board.[16] At that time, the Glassco proposals had mandated the President of the Privy Council to be the Acting Chairman of the Treasury Board. The proposals provided for greater specialization of roles between the three central agencies; an issue which was addressed later by the Lambert Commission. More generally, between the

1960's and the 1970's new ministerial portfolios were created for Supply and Services, the Treasury Board, and the President of the Privy Council. The extent to which functional specialization had occurred between the Department of Finance, the Privy Council Office and the Treasury Board was reflected later in Richard French's identification of three distinct planning systems in Ottawa: the Privy Council Office Planning System, the Treasury Board Planning System, and the Department of Finance Planning System.[17] The Privy Council Office is concerned with the formulation of priorities. The Treasury Board Secretariat is concerned with the management of personnel and financial issues. The Department of Finance is concerned with economic analysis and the formulation of fiscal policy. From the standpoint of management theory, these responsibilities appeared to be very distinct and unambiguous. However, the debate over public budgeting which took place between the 1960's and the 1980's demonstrated that there were major conflicts between the participants; the Department of Finance, the Privy Council Office and the Treasury Board, among others.[18] Consequently, there has been a structural dimension in the debate concerning public budgeting which is addressed in this paper. Perhaps the most significant issue was related to the question of which agency should take ultimate responsibility for budgeting; Finance, Treasury Board, the Privy Council Office or the Prime Minister's Office. Subsequent developments have demonstrated that while the Prime Minister is a key player in the process, he must have confidence in his Ministers of Finance and the President of the Treasury Board. It has been further demonstrated that broad political priorities must be established by the Prime Minister's Office and the Privy Council Office.

CHART 2

2.4 The Privy Council Office, the Cabinet Committee System, and the Changing Priorities of the Government of Canada

The Privy Council Office has been structured around two fundamental roles: plans and operations.[19] It is the focal point for a system of cabinet committees. Between the late 1960's and the mid-1970's a cabinet committee system evolved which played an important role in the making of policy and expenditure management decisions. Perhaps the most important reform was the creation of the Cabinet Committee on Priorities and Planning. It is concerned with the establishment of priorities.[20]

The number of cabinet committees have varied considerably since the 1960's. They reflect the shift in priorities. The number of committees increased during the Trudeau years to a maximum of approximately fourteen. The number of committees have oscillated between nine and fifteen during the Mulroney years.[21] The role of cabinet committees in expenditure management is an important element in the evolution of the expenditure management system. In this regard, it should be emphasized that the introduction of PEMS in 1981 was a major step in the evolution of the system in that it integrated the roles of the cabinet committees housed in the Privy Council Office with the financial management system controlled by the Department of Finance and the Treasury Board Secretariat. The creation of the Ministry of State for Economic and Regional Development (MSERD) and the Ministry of State for Social Development introduced new players into the system. Their presence impinged on the role of the Treasury Board Secretariat. The introduction of the Office of the Comptroller General in 1978 added new financial and evaluation responsibilities designed to strengthen the system. The structure and orientation of the Treasury Board Secretariat and the Office of the Comptroller General are discussed below in terms of their roles in expenditure management. The changed orientation of the cabinet committee system can be better appreciated by comparing the titles and roles of the committees established during the Pearson, Trudeau and Mulroney leadership years.[22]

On September 17, 1984, the then new Prime Minister Brian Mulroney announced his Cabinet, including a number of new ministerial positions and the changes in portfolio responsibilities (Chart 3). He also announced changes in Cabinet organization and the decision-making system. The role of the Operations Committee was altered during the 1980's. The changes made to this Committee had set the stage for the establishment of the Expenditure Review which was introduced in 1989.

It cannot be overemphasized that central to the whole decision-making process is the delegation of authority to ministers and cabinet committees. The system operates through the delegation of authority to central agencies, line departments, boards and commissions. The central agencies and line departments are linked through a number of cabinet committees which have been modified by each Prime Minister to satisfy the priorities established. Consequently, a comparison of the cabinet committee system established by Trudeau and Mulroney demonstrate major shifts in priorities and in the system of expenditure management.

The cabinet committees announced by the Right Hon. Brian Mulroney on September 17, 1984, were as follows:

(1) Cabinet Committee on Priorities and Planning; Chairman, Right Hon. B. Mulroney;
(2) Cabinet Committee on Economic and Regional Development; Chairman, Hon. S. Stevens;
(3) Cabinet Committee on Government Operations; Hon. R. de Cotret;
(4) Cabinet Committee on Legislation and House Planning; Hon. R. Hnatyshyn;
(5) Cabinet Committee on the Public Service; Right Hon. B. Mulroney;
(6) Cabinet Committee on Security and Intelligence; Chairman, the Right Hon. B. Mulroney;
(7) Cabinet Committee on Social Development; Chairman, Hon. J. Epp;
(8) Special Committee of Council; Chairman, Hon. E. Nielsen; and
(9) The Treasury Board; Chairman, Hon. R. de Cotret.[23]

Between 1984 and 1988 a number of changes were made to the cabinet committee system which demonstrated significant adaptation to international and domestic environmental changes. By February 1987, there were approximately eleven cabinet committees including new ones dealing with Communications, Privatization, Regulatory Affairs and Operations, and Foreign and Defence Policy.[24] There was an attempt in the early agenda of the Conservative government to increase defence spending and to decrease the allocation of resources to environmental control. The tabling of the document

CHART 3

Agenda for Economic Renewal signalled a shift in economic priorities.[25] The names of the cabinet committees and the orientation of the Government reflected a response to the changed international and domestic environment. It should be noted that earlier initiatives by the Liberals had already signalled a turn in orientation. For instance, the Liberals had released a policy paper entitled Economic Development for Canada in the 1980's that heralded a more market-oriented approach to policy and with less reliance on government intervention.[26] The Liberals had established a Board of Economic Development Ministers in 1978 in an attempt to emphasize economic development. In retrospect, the period between 1978 and 1984 depicted a shift toward economic growth. The G7 meetings which have taken place since the 1970's further demonstrated a trend toward coordinating economic policy initiatives in a more global setting. The reorganization of the Department of External Affairs in the 1980's was another illustration of this trend. It was mentioned earlier that the Department of Finance was reorganized in 1984 to reflect the changed environment.

2.5 The Performance of Political and Financial Management Roles in Expenditure Planning: The Significance of the Fiscal Plan

The establishment of the Cabinet Committee on Priorities and Planning meant that major emphasis was placed on the formulation of political priorities referred to elsewhere as "political management decisions".[27] As described above, an elaborate system of cabinet committees was established between the late 1960's and the mid-1970's. The Cabinet Committee on Priorities and Planning, the Treasury Board and the Cabinet Committee on Economic Policy performed important roles in the system. The Treasury Board and the Department of Finance were assigned more specialized roles within the expenditure management system. The subsequent review by the Lambert Commission suggested that inadequate attention was given to the "guardian role" (financial management) which should have been performed by these two agencies; the Department of Finance and the Treasury Board Secretariat.[28] To this end, the roles of these two agencies will be examined below. Donald Savoie has utilized a framework of guardians versus spenders to explain the operations of the expenditure management system. The guardians were few while the spenders were numerous.[29] His analysis suggests that the spenders were more successful than the guardians. The Royal Commission on Financial Management and Accountability was a major force which recommended a shift in the system which had operated until the late 1970's. It will be demonstrated below that steps were taken in the 1980's and 1990's to reverse this trend with the creation of the Expenditure Review Committee and the introduction of the Expenditure Control Plan (ECP).

One of the central recommendations of the Lambert Commission was the concept of a Fiscal Plan. The Commission suggested that political priorities should be formulated within the context of a long term fiscal plan. In this regard, it assigned a lead role to the Department of Finance which must be seen as the guardian of the fiscal strategy. In retrospect, the Department of Finance was significantly reorganized in 1984 and the subsequent appointment of Michael Wilson as Minister of Finance led to a major change in the role of the Department in fiscal policy management. Michael Wilson has been the longest serving finance minister since World War II. The Department of Finance emphasized the need to formulate a strategy to deal with the deficit. There was also major initiatives to reform the tax system. In many respects the Lambert Commission had advocated such a strategy. These developments taken together constituted a major effort to establish an integrated fiscal strategy for the federal government. The Department of Finance has had relatively stable leadership at the ministerial and deputy ministerial levels during the 1984 to 1993 period relative to the period of turbulence which existed during the 1970's.

3. THE TRANSITION FROM THE 1970's TO THE 1980's: THE IMPACT OF THE LAMBERT COMMISSION ON FINANCIAL MANAGEMENT AND ACCOUNTABILITY

3.1 The Lambert Commission, the Department of Finance and the Fiscal Plan

The roles performed by the Department of Finance and the Treasury Board in the expenditure management process have been subjected to critical review. The Lambert Commission on Financial Management and Accountability identified fundamental flaws in the system. Essentially, the Commission argued that the roles of the Department of Finance and the Treasury Board had been downgraded. Their conclusion suggested that greater emphasis was placed on the performance of "political management" rather than on "financial management" roles. The Government of Canada responded with the Policy and Expenditure Management System (PEMS) which was an attempt to integrate the policy and the expenditure management systems. However, the reforms turned out to be less effective than was anticipated in that it had also integrated the roles of the spenders and the guardians.[30] The guardians are represented by the Department of Finance and the Treasury Board. One of the major criticisms levelled against PEMS was that it was too cumbersome. It generated a considerable amount of redtape. There was a small book of rules of the game. Much effort was made by spending Ministers to use the rules to get around spending limits. As a result, central agencies had to spend much time trying to close loopholes.

The Lambert Commission had outlined a framework for a mutually compatible management system. In the words of the Commission:

> The establishment of a "mutually compatible management system appropriate to the requirements of government" begins at the centre. It is the Ministry as a whole, the Government, that must establish and direct the processes, organization, and structure that govern the operations of the myriad departments, agencies, Crown corporations, and other bodies which carry out the day-to-day business of the Government of Canada. In

> subsequent sections of our Report, we deal with management within departments and agencies; with management in government. Before doing so, however, it is essential to establish the fundamental framework within which those constituent parts should operate. This requires a determination as to how the Ministry as a collectivity that forms the centre should be organized and how it should function in order to provide the most effective management of government.[31]

The Commission went on to assert the following:

> Essentially, our proposals are based on the related convictions that responsibility at the political level for the subject matter of the Fiscal Plan can only be vested in the most senior of Cabinet committees, that of Priorities and Planning under the chairmanship of the Prime Minister; second, that responsibility for establishing the government's fiscal position cannot be divorced from responsibility for setting expenditure limits for departments and agencies; third, that there must be a single focus for the Government's collective management responsibility; and, fourth, that the Fiscal Plan must be based on the best available information about the Government's priorities and objectives and the possibilities that exist for realizing them, both in terms of what the economy can support and of what can be done within government.[32]

Because financial considerations must become a matter of paramount concern, the Department of Finance, as the central agency with primary responsibility for economic management, should be assigned the lead responsibility for the development of the Plan and for the fiscal position of the federal government. The Plan should be developed in concert with the secretariats of a reconstituted Treasury Board and the Privy Council Office, forming a closely knit team. The Plan should be submitted to the Cabinet Committee on Priorities and Planning with the full backing of the ministerial heads of these agencies. It is significant to note that the Lambert Commission had recommended a highly integrated system of financial management significantly controlled by the guardians.

The Lambert Commission had indicated that fundamental to a sound management of government is the development of a medium-term Fiscal Plan for the achievement of priorities and objectives. Such a plan would constitute a political and managerial commitment to the achievement of goals. Its publication would display clearly the effects on expenditures of changes in priorities, and its existence would provide assurance to the different levels of government, business, and international communities, and the Canadian people that the financial consequences of the federal government's intentions had been fully recognized and assessed.

The need to determine the availability of resources before expenditures are proposed, the financial interdependence of the three levels of government in Canada, the size and extent of shared-cost programs, and the ever increasing influence of economic factors beyond Canada's direct control led the Commission to conclude that a Fiscal Plan for Canada based on clearly stated economic assumptions should include both revenue expectations, based on existing taxation legislation and all planned expenditures. It should cover a period of five years. This is the minimum commitment required to make it useful to planners and to provide sufficient time for testing new initiatives. It should also be the maximum time needed to wind down in an economical and coordinated fashion any programs judged obsolete or redundant, or to transfer responsibility to other levels of government where appropriate.[33]

Placing responsibility for taking the lead in the development of the Plan in the Department of Finance would unite the tasks of revenue-raising, establishing functional expenditure limits, and debt management under one roof. This would provide the means to ensure that the medium-term consequences of program proposals are given adequate consideration and that revenue-raising and economic management programs are coordinated and coherent. Assigning the Comptroller General responsibility for proposing departmental and agency expenditure limits within established functional limits would help to ensure that managerial competence becomes an important consideration in determining to whom the taxpayers' resources should be entrusted. The participation of the Privy Council Office from the beginning of the planning process would ensure that the plans developed meet the test of being "mutually compatible" with and "appropriate to the requirements of government". While we appreciate that it is not always easy for separate central agencies to coordinate their activities, the essence of this proposal is that they must, and that the deputy heads of the central agencies must be held accountable to Cabinet for its achievement. The Fiscal Plan would be integrated into the parliamentary process. Accordingly, the Commission emphasized that:

> The Fiscal Plan would be presented to Parliament annually and referred to a new committee of the House of Commons, the Standing Committee on Government Finance and the Economy, in order to provide Parliament with the opportunity to focus on total government revenues, expenditures, the fiscal balance, and the public debt as they relate to present and projected economic conditions and the broad priorities of the Government. Committee consideration of the Fiscal Plan over a period of some weeks would enable both government and non-government organizations to contribute to the discussion of the economic and social implications of the Plan and the priorities associated with it. A subsequent report by the Committee to the House would provide the basis for a short debate, during which it would be open to the Government to indicate any changes it was prepared to make in the Plan in light of previous discussions in committee or other public forums. The Plan should not be regarded as a matter of confidence, however, and should not be subject to a vote at the conclusion of the debate.[34]

In retrospect, the most significant change to the system occurred in the mid-1970's. The 1973-75 external shocks to the system led to a number of institutional reform proposals.[35] The change in the Government's fiscal position, the identification of financial management problems by the Auditor General, the establishment of the Lambert Commission, the recognition of weaknesses in the institutional arrangements and the absence of strong financial and evaluation procedures led to a number of reform proposals in the late 1970's.[36] Let's review a few stages in the evolution of the budgeting system which is in operation in the 1990's.

The economy in general and the fiscal position of the Government of Canada changed in a dramatic way in the early and mid-1970's. Consequently, it is most important to capture the manner in which the Department of Finance perceived the economic situation in the mid-1970's and the mid-1980's. While the Auditor General was concerned with tight financial management and control, the Department of Finance was concerned with the necessity to change the system of economic management. The Department had recognized that the period of strong growth which had existed between the 1960's and the 1970's had ended. At the same time, inflation had become a serious problem. Wage and price controls were introduced and changes were made to the Established Programs Financing Act in 1977. The changes made by the Liberals in the late 1970's were indicative of the even stronger initiatives taken later by the Conservatives in 1984 with the release of Agenda for Economic Renewal. In short, the Department of Finance was responding to very significant changes in the international and domestic economic setting which warranted a shift in its fiscal policy. It will be demonstrated later, that even stronger measures were adopted in 1989 with the establishment of the Expenditure Review Committee. The institutional reforms intensified between the 1970's and the 1980's.

3.2 The Fiscal Significance of the Mid-1970's: The 1975 Budget: Toward A New System

The economic environment changed significantly in the mid-1970's. The changes have required the establishment of new institutional arrangements. The following developments should be identified and appraised.

First, the 1975 federal budget indicated that the fiscal environment had changed and that new expenditure management initiatives had to be taken. One consequence of this recognition was the passage of the Established Programs Financing Act, 1977.

Second, the Auditor General's report of 1976 indicated that the financial management system was chaotic. In no uncertain terms, he warned that he was "deeply concerned that Parliament and indeed the Government - has lost, or is close to losing effective control of the public purse."[37]

Third, the Lambert Commission was established to critically review the system. It identified flaws in the system enumerated below which led to the strengthening of the roles of the Treasury Board and the Department of Finance in the expenditure management system, given the emphasis placed on the fiscal plan. However, the reforms which were introduced in the late 1980's, with the creation of the Expenditure Review Committee discussed later, demonstrated that the 1979-1984 Envelope System Reforms were inadequate.

Fourth, at least five flaws were identified by the Lambert Commission. They were indicative of the deficiencies in the system which had developed between the 1960's and the 1970's: first, while Glassco had recommended the decentralization of authority, virtually no effort was made to establish clearly defined objectives against which performance should be measured; second, the management of personnel was considered to be as important as financial management but it was impaired by the delegation of responsibilities to both the Treasury Board and the Public Service Commission; third, the roles of the Department of Finance and Treasury Board had been downgraded relative to the Privy Council Office with the evolution of the cabinet committees; fourth, the proliferation of crown corporations and boards had led to a significant need for important controls on these organizations; and fifth, major managerial problems had developed from the failure to clarify the roles of Deputy Ministers within departments. The Commission recommended the establishment of a mutually compatible management system to correct the flaws identified above. One aspect of the reform dealt with the manner in which the estimates were submitted to Parliament. The Lambert Commission implied that the Glassco Commission assertion, let the managers manage, had been misinterpreted. The changes suggested that political modifications had been made to the managerial principles outlined by the Commission. The Lambert proposals and the manner in which they were implemented suggests that there are always political forces which alter the manner in which proposals are implemented and that budget reforms must address political issues and concerns.

Fifth, by the mid-1970's, the Auditor General had called for the establishment of the Office of a Comptroller General separate from the Treasury Board Secretariat. The subsequent contributions of the Office of the Comptroller General to effective public sector management need to be critically reviewed. It must me examined and discussed as part of the evolution of the Treasury Board. The evolution of the Treasury Board Secretariat can be considered in two stages. First, there were the initial developments between the 1960's and the 1970's. During this period, the Board's managerial responsibilities were adjusted to accommodate added responsibilities. Second, there were the developments in response to the demands for more effective program evaluation. This was reflected in the creation of the Office of the Comptroller General in the late 1970's. The divisions established within the Office of the Comptroller General depict the initiatives taken to improve financial management and program evaluation. Consequently, the system of financial management is reflected in the structure and operation of the key central agencies, the Department of Finance, the Treasury Board Secretariat and the Office of the Comptroller General. They are key structures identified by the Lambert Commission in what it considered as a mutually compatible management system. The Office of the Comptroller General has been a source of reforms in the various departments. In fact, comparable positions were established within each department; a development which may lead to increased decentralization of financial management and control in the 1990's.

3.3 The Central Agencies and Financial Management, The Role of the Treasury Board and Its Secretariats

The Treasury Board of Canada has emerged as a major participant in the Expenditure Management System concerned with financial and personnel management. Since the late 1970's, the Board's Secretariat has been restructured and divided into two components: the Treasury Board Secretariat and the Office of the Comptroller General. The Treasury Board Secretariat has been responsive to pressures in the international and domestic environments. This is reflected in its changing structure.

In the mid 1960's, the Treasury Board Secretariat was organized into three distinct components: the Program Branch, the Personnel Branch, and the Administrative Improvement Branch. The introduction of Collective Bargaining in 1967 led to the establishment of a Staff Relations Branch. In 1969, the Treasury Board issued the Program Guide and the PPBS was adopted. The endorsement of planning led to the adoption of a Planning Branch. The earlier introduction of bilingualism had led to the establishment of a Bilingualism Branch. By the end of the 1980's, the Treasury Board Secretariat included the following

branches: Bureau of Real Property Management; Administrative Policy; Program; Personnel; Staff Relations; Official Languages; and Administration
(Chart 4). By the early 1990's, a Human Resources Branch was established to deal with staff development. Thus, the Treasury Board Secretariat has clearly responded to various managerial challenges by adapting its structure. It will be demonstrated below that further changes were made in the late 1970's and the early 1980's to the Office of the Comptroller General which absorbed sections from the Secretariat. From the point of view of expenditure analysis, it is the Program Branch which provides the

CHART 4

link to the departments in the preparation of the estimates.

In the early 1990's, five branches within the Treasury Board oversee the broad management functions of the government. They are as follows; Administrative Policy, Official Languages, Personnel Policy, Program and the Human Resources Development Branch. However, it is the Program Branch which is significantly involved in budgeting. Consequently, a review of its responsibilities provide important insights to the budgetary process. The role of the Program Branch is to undertake the following:

- To make recommendations to Treasury Board ministers on allocation of the government's financial and person-year resources in the light of government priorities and results achieved.
- To make recommendations to Treasury Board ministers on the accountability frameworks (Program Activity Structures) within which Parliament approves resources and departments and agencies report on their use of resources to Treasury Board and to Parliament.
- To coordinate preparation of the Estimates (Parts I and II of Main Estimates as well as Supplementary Estimates) and coordinate the process whereby the government obtains Supply from Parliament.
- To monitor the implementation of approved programs by departments and agencies and advise the Treasury Board on their success in achieving intended results.
- To promote innovative management and increased effectiveness and efficiency in program delivery through initiatives such as IMAA (Increased Ministerial Authority and Accountability) and Special Operating

Agencies (SOA).

- To advise the President of the Treasury Board (in his role as member of Cabinet committees) on the resource and management implications of new policy and project initiatives.

The Program Branch undertakes the following functions:

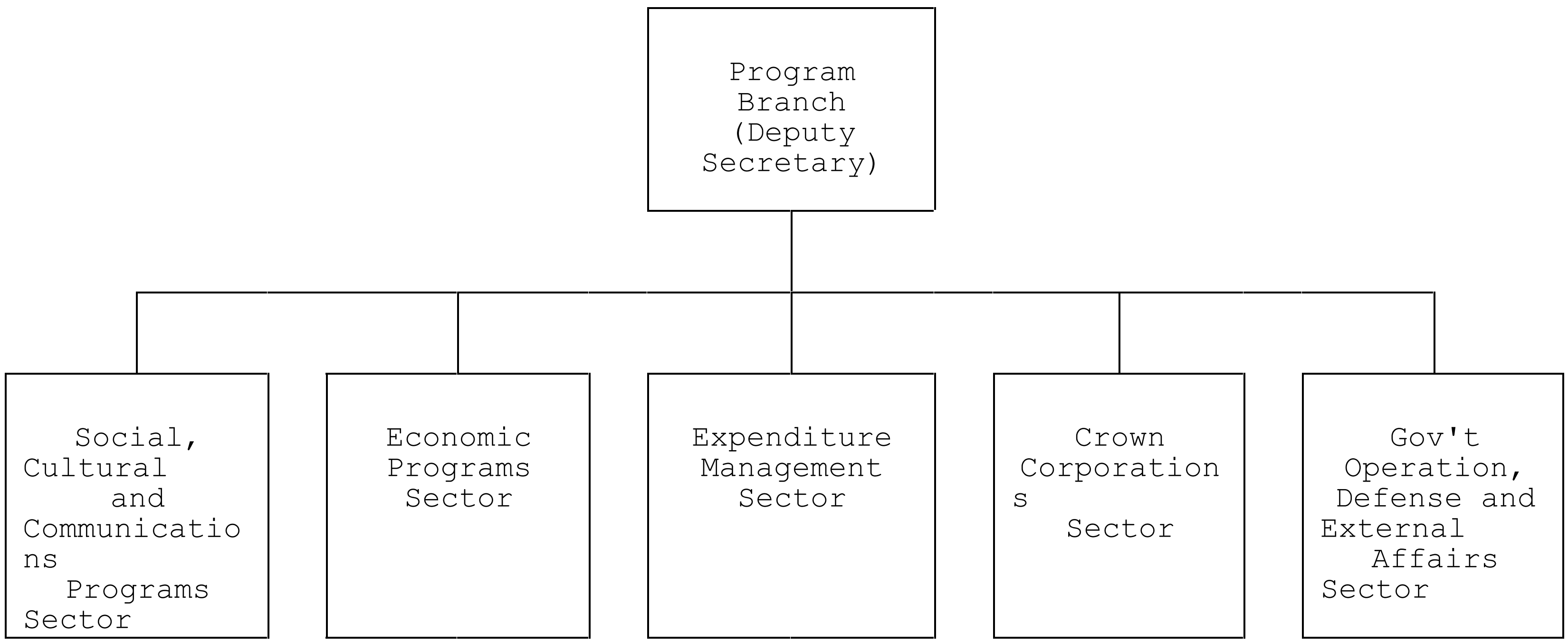
- It coordinates the annual multi-year operational planning and Estimates with the government's Budget exercise.

- It assesses the plans and proposals of individual departments and agencies for their resource implications and impact.

- It acts as liaison between Crown corporations and central government agencies in matters of policy and resources.

The Branch is organized in a manner which reflects the broad functional areas of government as displayed in Chart 5:

CHART 5
PROGRAM BRANCH OF THE TREASURY BOARD SECRETARIAT



The Branch carries out its responsibilities under the five main functional areas shown above.

There are three program sectors responsible for assessing departmental policies and programs, one central sector that coordinates the annual planning and Estimates process with the government's Budget exercise and one sector to advise on the policies and legislation that govern Crown corporations and their corporate plans and budgets.

The work of the Program Sectors is divided among three Assistant Secretaries: the Assistant Secretary - Economic Programs, the Assistant Secretary - Social, Cultural and Communications Programs and the Assistant Secretary - Government Operations, Defence and External Affairs.

In order to capture the manner in which the accountability system which exists in the 1990's evolved, it is necessary to review the influence of the Lambert Commission on the reform of financial management and accountability. This issue is addressed below.

3.4 Enhancing Accountability in the Financial Management System

The Lambert Royal Commission on Financial Management and Accountability made several recommendations designed to improve the system of accountability in government. The Trudeau government responded with a document entitled Accountable Management. Essentially, the Government and the Treasury Board adopted the following comprehensive reform strategy:

1) the concept of a fiscal plan;
2) a discipline on the resource allocation process related to the fiscal plan;
3) accountability of government to parliament;
4) accountability within government;
5) accountability and efficiency in the administration of financial systems;
6) accountability and efficiency in human resource management; and
7) a continuing strategy for reform.[38]

It is demonstrated below that the system of reporting expenditures to Parliament was subsequently reformed and presented as The Expenditure Plan, Parts I, II and III. It was a more informative system than that which had existed before.

The Lambert Commission had defined accountability in a very specific way. The Commission linked accountability to the achievement of public confidence in the public service. The words of Arnold Heeney were quoted:

In a complex society which makes ever-increasing

> demands on government, a large and complicated public service is inevitable. Great size and complexity carry with them terrible dangers, chiefly, of course, the dangers commonly associated with the word 'bureaucracy'. Individual civil servants may lose - or may never acquire - the sense of vocation which is so important to the quality of human achievement. They may well feel themselves to be without purpose in a massive government machine. Should this happen, able men and women will not be persuaded to enter the Public Service. To prevent this happening should be the continual care, not only of government, but of all Canadians.[39]

Public confidence will return with the assurance that public servants are managing soundly and being held accountable for performance and results. The Commission adopted the position that accountability, "like electricity, is difficult to define, but possesses qualities that make its presence in a system immediately detectable. To touch a live wire in a circuit is enough to establish the presence of electricity without further need of definition". The shock of recognition that attends the presence of accountability in a system of government may not be quite as direct, but it is nonetheless detectable. More specifically, the Commission stated:

> We see accountability as the activating, but fragile, element permeating a complex network connecting the Government upward to Parliament and downward and outward to a geographically dispersed bureaucracy grouped in a bewildering array of departments, corporations, boards, and commissions. Accountability moves through this network like the current in a circuit but always in some sort of relation to the control centre, the Cabinet.
>
> The dispersal and structural complexity of the bureaucracy make the control centre vulnerable to

> stoppages and short-circuits or overloading. The control centre, the Government, although ultimately responsible for answering to the legislature, may find itself out of touch with what is happening, or failing to happen, at the other end of the network. Similarly, a signal from the centre may never reach the departmental unit or agency concerned or may reach it in so confused a state that judgements as to performance become impossible to make.[40]

The Lambert Commission indicated that four departments and agencies were responsible for central management: the Treasury Board and its twin secretariats, under the leadership of the Secretary of the Treasury Board and the Comptroller General; the Department of Finance; the Privy Council Office; and, the Public Service Commission. Each is expected to give general direction to managers in government by providing central guidance and services to individual departments and agencies involved in the operation of programs and activities. The Commission simultaneously indicated that the central agencies should not usurp the individual responsibilities of departments and agencies for the management of their affairs. Consequently, the Commission attempted to clarify the roles of the central agencies. The Government of Canada responded to the Lambert Commission report with the Policy and Expenditure Management System and with Accountable Management mentioned above. An important element in the government's response to increase accountability was reform of the estimates. This is discussed in section 5.4 below.

3.5 The Privy Council Office and the Policy and Expenditure Management System: The Integration of Political and Financial Priorities

In 1981, the Privy Council Office published a paper which utilized "the systems framework" to outline a Policy and Expenditure Management System designed to integrate various components of the Canadian public administration system. The document indicated that:

> the fundamental purpose of the new system is to ensure greater ministerial control over the management of policies and expenditures. It seeks to do this by integrating the processes of policy-making and fiscal expenditure planning within the Cabinet Committee system.[41]

The Policy and Expenditure Management System was introduced when resources were, relatively speaking, available. The document stated that:

> the objective is to ensure that policy and program decisions are taken with an understanding of and responsibility for the government's policies and priorities. Objectives and resources are inextricably related and the requisites of rational decision-making require that they be considered together within the new system.[42]

PEMS was regarded as a major development in a system which had evolved between the 1960's and the 1980's. By the mid-1980's, a complex financial management system had evolved. Some critics considered the system to be too complex. Consequently, initiatives were taken by Prime Minister John Turner to simplify the system. The abolition of the ministries of state for Economic and Regional Development and Social Development represented one aspect of the reform designed to simplify the system.

By 1984, the cabinet committees and the system of envelopes were depicted in the Expenditure Plan as displayed in Chart 6.[43] The Policy and Expenditure Management System was, as the name suggests, a marriage of the policy-making and expenditure management systems. It was an attempt to force politicians to consider the budgetary implications of their actions. The system actually had a number of aims. These have been described by the then President of the Treasury Board as follows:

> 1) to achieve closer integration of the government's priority-setting, policy development and expenditure management decision-making processes;
> 2) to decentralize decision-making authority, in recognition of the increasing range and complexity of government responsibilities and the interrelated policies and programs designed to discharge them;
> 3) to increase ministerial discretion and control over the policy, planning and expenditure decisions of the government; and
> 4) to provide an adequate time frame in the planning process, so that ministers can review existing policies and programs and bring about desirable changes in the use of resources to reflect changing priorities of the government.[44]

Prime Minister Trudeau's use of PEMS involved quite a lengthy and complex budget process. The Department of Finance prepared a five-year fiscal framework, which it updated each year. This was communicated to the Cabinet Committee on Priorities and Planning, which used the information to decide on the total level of government spending for a particular year, and then divided that pie into broad categories such as social affairs, economic development, external affairs, and defence. The "envelopes" which contained these allocations were then passed to the relevant policy committee to further divide between departments and programs.

PEMS also involved the individual departments in the planning process. Strategic Overviews had to be prepared and submitted to Cabinet for approval. Multi-year operational plans were also required. New Cabinet Secretariats under the Ministry of State Economic and Regional Development (MSERD) and the Ministry of State for Social Development (MSSD) were created to manage the process and the "envelopes." It was indeed a very elaborate and complex process.

CHART 6

Sometimes, an "envelope" contained a "policy reserve". This was a pool of funds that the policy committee could use at its own discretion to launch new initiatives. Policy committees could create or add to their policy reserves by reducing expenditure on existing programs. There was also the possibility of a negative policy reserve, which would force the committee to search for savings in its area. One of the most significant innovations of this system was the power it gave to the policy sector Cabinet committees to make budgetary and policy decisions in their sectors, as long as they stayed within their set expenditure limit.

In theory, envelopes were supposed to reflect not only cash expenditures, but also to include tax expenditures. In practice, however, tax expenditures were never really integrated into the system. The Minister of Finance kept the sole prerogative to implement tax measures, but was required to seek the concurrence of the appropriate program minister and cabinet committee if the measure related to a specific program area. The revenue costs or savings of particular tax measures originating from the Minister of Finance were not to be automatically debited to the expenditure envelopes, although they could be reflected in the setting of expenditure targets for future years. But if a program minister proposed a tax expenditure, it was supposed to be debited to the committee's policy reserves. This actually happened in only one case namely for the continuation of an accelerated deduction for metric conversion units beyond its expiry date. In contrast, when the system for tax expenditures was first established, much time was wasted initially by program ministers on cabinet committees trying to get envelope reserves credit for the elimination of tax expenditures so they could introduce new spending programs financed in effect by tax increases. These efforts were successfully resisted by the Minister of Finance. The rules for the incorporation of tax expenditures in the expenditure management system resulted in a temporary decrease in demands for new tax expenditures by program ministers. But they were abandoned in the mid 1980's for a number of reasons, including, most notably, their complexity and arbitrariness. [45]

The major innovation of PEMS was breaking up the former game of spenders and guardians. Under PEMS, five committees were responsible for expenditure review; Priorities and Planning, Treasury Board, Social Development, Economic and Regional Development, and Foreign and Defence Policy. Another innovative aspect of this system was that it showed that there was no bottomless pot to which departments could keep returning to request additional funding for new policy initiatives. If individual departments or ministers wanted to embark on new programs, they would have to find the needed funds in their "envelope". This meant cancelling or rearranging existing programs or making them operate more efficiently so that new money could be made available. Instead of the game of spenders vs. guardians, departmental ministers were now forced to be both spenders <u>and</u> guardians. In retrospect, this assumption is rather debatable and the subsequent reforms demonstrate that the system did not work very well.

The most basic problem with PEMS was, quite simply, that it had not been effective in limiting expenditure. In particular, ministers were neither able to come to grips with "X" budgets, nor had they ever seriously considered major cuts in statutory appropriations. These are permanent appropriations, made under legislation for such items as old age security, family allowances, and fiscal transfers, other than the annual estimates. Expenditure on these items has been approved under other legislation and does not require annual approval. However, since statutory appropriations make up over 60 percent of the total budget, it is clear that any attempt to reduce spending must examine these programs carefully. This involves more direct involvement by ministers and departments.

In sum, instead of ministers becoming both spenders and guardians as was hoped, ministers still continued as spenders, but forgot about being guardians altogether. Experience would seem to suggest that the control of public spending requires centralized decision-making and can not be satisfactorily delegated to cabinet committees responsible for specific functional areas. The Prime Minister and Cabinet must change the mandate of departments. The foregoing points to the interplay between political, economic and managerial roles in budgeting. Public budgeting reforms are a function of prime ministerial strategic leadership.

3.6 Prime Ministerial Leadership and Expenditure Management: Responding to International and Domestic Environmental Forces

The reforms between the 1960's and the 1980's shows that budgeting systems have emerged in response to a combination of environmental demands and political leadership response. From this perspective, PPBS, PEMS, and other reforms should be critically evaluated in terms of the interaction between the Government of Canada and a rapidly changing international and domestic environment. This analysis is based on the premise that political parties and political leaders respond to these forces. Each Prime Minister has responded to a particular set of forces which led to specific reforms. Organizations such as the Privy Council Office, the Treasury Board Secretariat and the Department of Finance were all affected. Prime Ministers perform key roles in altering the appointment process and in the delegation of authority to ministers and departments that shape the way these organizations function. In some cases it had led to the creation of new organizational forms such as special operating agencies.

Budgetary reforms require strong political leadership.

Obviously the Prime Minister must play a lead role in this process. Prime Minister Lester B. Pearson introduced major social reforms which had long-term expenditure implications for the system. There was the post-war baby boom which led to the adoption of programs affecting health, education and welfare. Prime Minister Pearson had also implemented the Glassco Commission recommendations. Prime Minister Trudeau expanded the cabinet committee system, introduced PPBS and rationalized the roles of the central agencies. He later integrated the policy and expenditure management systems in the early 1980's. Prime Minister Brian Mulroney entered the system when there was a feeling that the government had become too large and complex. One of the most significant changes during Brian Mulroney's leadership was the continuity in ministerial and deputy ministerial leadership at the Department of Finance. Between the 1970's and the 1980's the Department of Finance was led by the following ministers; John Turner, Donald Macdonald, Jean Chretien, John Crosbie, Allan MacEachen and Marc Lalonde, all Liberals with the exception of John Crosbie. Between 1984 and 1992 the department was led by two strong ministers, Michael Wilson and Donald Mazankowski. Accordingly, each Prime Minister has influenced budgeting in a fundamental way by putting his own distinctive stamp on the system. In turn, each Minister of Finance has influenced the process in his own way. Consequently, this study demonstrates that personalities have influenced the reform of budgeting.

The system was also influenced by philosophical changes in budgeting. PPBS was introduced to change the classical budgeting system which operated until the 1960's.[46] It treated the expenditure base as given. Classical budgeting focused on additional inputs rather than on program objectives. It was hoped that PPBS would introduce a top down system of budgeting, but its lasting legacy was more in the way the estimates are presented as programs. The ineffectiveness of PPBS in restraining spending can be gauged by the extremely rapid growth in government spending between 1970 and 1975. Ida Hoos suggests that it was a good system for establishing spending priorities.

Prime Minister Trudeau's attempt to make a major reduction in government spending was most clearly reflected in 1978 when he announced spending cuts on national television following his Bonn Summit without consulting the President of the Treasury Board and the Minister of Finance.[47] His action was taken outside of the formal budgetary process and it was dissatisfaction with this approach which led to the development of a new system (PEMS).

Trudeau's dramatic cuts, combined with the concerns expressed by the Auditor General in 1976 that parliament and indeed the government, had lost or was close to losing control of the public purse and the recommendations of the Lambert Commission led the federal government to introduce PEMS which was heralded as having much promise for curbing growth in spending.

Initiatives to cut spending were taken in 1975, 1976, 1978, and in 1979. The Policy and Expenditure Management System was introduced as a comprehensive reform package in contrast to the various ad hoc initiatives listed.

PEMS operated within the framework of cabinet committees. Cabinet committees were granted spending envelopes or expenditure limits and a policy reserve to be spent on new initiatives. If ministers and cabinet committees wanted to approve new spending, beyond what was available in the policy reserve for new initiatives they would have to make cuts in existing programs to free up resources. In theory, PEMS placed responsibility for savings squarely on the shoulders of those who spend.

PEMS also expanded the spending horizon by making spending projections by envelope available for four years into the future. New central agencies were established to assist the policy committees and mirror committees and deputy ministers were asked to review all proposals coming forward for funding from policy reserves. It will be demonstrated below that the system was not as successful as was anticipated.

It will be demonstrated below that the system was not as successful as anticipated. It is worth pointing out that the Department of Finance was reorganized in 1984 in response to the changing international and domestic environment. The reorganization followed changes in External Affairs and Industry, Trade and Commerce. Consequently, there was a major shift in economic and expenditure policies. Greater emphasis was placed on deficit management. The role of the Department of Finance was significantly strengthened after 1984.

3.7 Expenditure Planning and the Nielsen Task Force: Toward A Reformed Financial Management System

Since 1984 when the Conservatives came to office, the government has consistently pursued a market-oriented agenda emphasizing expenditure restraint and deficit reduction. The strategies are in contrast to those of the 1960's and the 1970's.

The Conservative government's approach was set out in its policy paper An Agenda for Economic Renewal published in November 1984 which established the framework for its subsequent policies.[48] The Agenda emphasized deregulation and privatization and on relying on the private sector as the engine of growth. A commitment was made to reduce the projected level of annual expenditures by 1990 by $10 to $15 billion. Finance Minister Michael Wilson set the goal at $15 billion by 1990-91. In November 1984, the first round of spending cuts were tabled. The Nielsen Task Force was given a specific mandate to review governmental programs. Between 1984 and 1988 many initiatives were taken to reduce public spending. The government also announced a commitment in 1986 to cut the number of positions in the public service by 15,000 person-years between 1986-87 and 1990-91.[49]

The Nielsen Task Force, more specifically, the Ministerial Task Force on Program Review (MTF), was the government's most comprehensive effort to review the existing programs with a view to eliminating those that no longer served a purpose and consolidating others in the hope that not only savings, but also better government, would result. The Nielsen Task Force succeeded in identifying a large number of management initiatives that would save the government money, but it disappointed those that had looked to the Task Force to identify large cuts in program spending and to muster the political support to see the cuts implemented. This was a political task that could not even be delegated to a Task Force chaired by the Deputy Prime Minister.

The Nielsen Task Force drew its members from the private and public sectors. The ministerial representation included the Minister of Finance, the President of the Treasury Board, the Minister of Justice and one spending minister. All of the study teams asked questions such as "Why is the federal government in this field? What should be its role?" The task forces recommended that programs should be cut back, suggested that some be decentralized, others should be privatized, while others should be contracted out. The nineteen study group reports were tabled on March 11, 1986. The overall review recommended one-time expenditure and tax reductions of between $7 to $8 billion. The study groups recommended substantial reduction in subsidies to agriculture, fisheries, transportation and business. One report urged the government to rationalize sales tax exemptions, terminate obsolete programs and cut back various direct subsidies. The study urged cuts in regional development programs and the abolition of the Federal Business Development Bank. One study recommended the elimination of virtually all agricultural subsidies, including those directed at dairy, feed freight, feed tax rebate. Another suggested that the government was investing poorly in training. The study recommended changes to government procurement policies.

One reviewer has indicated that the Nielsen Task Force findings became an exercise in search of support in government.[50] Many decisions were taken immediately after the reports were tabled, but no major programs were eliminated. Some analysts argued that the reports did not take into account the regional implications of expenditure reductions proposed. Overall the results were perceived to be relatively modest when compared with the unrealistic high expectations that had arisen. Why did the Nielsen Task Force fall short of expectations? In our view, it is because observers confused the technical task of analyzing government spending in order to identify potential savings with the political task of actually making the decisions to cut spending and mobilizing the support necessary to implement them. The expenditure reduction exercises which developed in the early 1990's were supported by influential sectors within the economy and the society. In this regard, the work of new organizations such as the Business Council on National Issues (BCNI) should be mentioned.

4. DEFICITS, GLOBALISM, COMPETITIVENESS AND THE PRESENT EXPENDITURE MANAGEMENT SYSTEM FOR THE 1990'S: CONTROLLING PUBLIC EXPENDITURES, THE EXPENDITURE REVIEW COMMITTEE AND THE EXPENDITURE CONTROL PLAN

4.1 The Establishment of the Expenditure Review Committee

One of the major preoccupations of the Mulroney government has been the reduction of the deficit. The commitment led to the establishment of an Expenditure Review Committee (ERC). This concern increased significantly in the government's second term, beginning in 1988. This has had a major impact on both the substance and the process of the budget. After the 1988 election, Prime Minister Mulroney decided that the only way to control expenditure was to centralize decision-making on the expenditure budget. Consequently, in 1989 under pressure of a deficit that refused to decline further, the Mulroney government announced a more comprehensive approach to expenditure reduction when it announced a new cabinet committee system. The changes signalled an end to the Policy and Expenditure Management System (PEMS). The Mulroney changes did away with the policy envelopes and shifted effective decision-making away from policy committees of cabinet to the Operations Committee, and to Priorities and Planning and to a new Expenditure Review Committee.[51] In effect, it has led to an inner and outer cabinet committee system.

Nearly all cabinet committees with the exception of the Treasury Board, which fulfils statutory duties, were placed under an enlarged cabinet committee on Priorities and Planning (Chart

7). All new spending decisions must be approved by Priorities and Planning. Authorizing program spending continues to be the responsibility of the Treasury Board. Before going to Priorities and Planning, new spending decisions must go through the Operations Committee which was originally chaired by the then Deputy Prime Minister Don Mazankowski. While the Operations Committee was established earlier, it was transformed to become, in effect, the gatekeeper of the Priorities and Planning Committee. It demonstrates, once again, how the cabinet committee system can be adapted.

Under the new system the policy committees of the Cabinet, particularly new ones dealing with the Environment, Economic Policy, Human Resources and National Identity, were to concentrate on policy and were freed up from having to handle routine transactions. Thereafter, the Treasury Board was expected to handle much of the routine work and only the Treasury Board and the Cabinet Committee on Priorities and Planning were mandated to authorize expenditures.

According to the government's press release, these changes in ministerial duties and Cabinet structure cleared the decks for the Government to prepare the program for its second mandate that was laid before Parliament in the spring of 1989. The streamlined Cabinet Committee System would enable ministers to concentrate on the development of the Government's key initiatives.

As a further step to permit the committees to concentrate on policy, their membership was streamlined. Each committee was given a more precise focus of responsibility and activity that was of direct and common interest to all members. The former broad sectoral committees were abolished, with the result that membership on individual committees was cut from as many as 22 or 23 ministers to the range of 8 to 12. The overall effect of the changes was to reduce the paper burden on ministers and permit them to concentrate on key initiatives.

The key task of controlling expenditures was assigned to two new Cabinet committees: Operations ("Ops") and Expenditure Review ("Chops"). The workings of these powerful committees merit more detailed discussion given their central role in the expenditure management system of the early 1990's.

The <u>Committee on Operations ("Ops")</u> is responsible for overseeing the agendas of the policy committees and may itself handle any item of business if the appropriate policy committee is not soon to meet or if the "Ops" ministers so choose. Since it effectively sets the agenda of the Cabinet, and since the one who sets the agenda gets to control priorities, "Ops" is a very powerful committee indeed. "Ops" was originally chaired by the Deputy Prime Minister and has a small membership chosen from among senior P & P ministers (members of the Cabinet Committee on Priorities and Planning) who also chair other committees. It is now chaired by the Government House Leader.

The mandate of the Expenditure Review Committee ("Chops") is to ensure that "the government's expenditures continue to be directed at the highest priorities and that expenditure control continues to contribute to the deficit reduction". It "screens all policy proposals which have expenditure implications before they can be discussed by policy committees". "Chops" was formally chaired by the Prime Minister, but in practice is usually chaired by the Deputy Prime Minister cementing its ties to "Ops".

"Ops and Chops", working together, were effective gatekeepers in the policy-making system. A new proposal had to get by "Ops" to get on the Cabinet agenda, and if the proposal required additional spending it also had to get through "Chops". These changes constitute a significant centralization of the system. While "Chops" was helpful in blocking new spending, it was less successful in identifying cuts in spending. This was a key factor that led to its ultimate demise as we will see later.

The Department of Finance still consults with the Treasury Board in recommending a fiscal plan, acting together as guardians vs. the spenders. The Treasury Board contributes information about "reference levels", i.e., the level of spending needed to continue existing programs at their current level. Finance then estimates the revenue likely to be generated in the coming year and provides some advice on the appropriate level of surplus or deficit needed to stimulate or slow down the economy. These recommendations constitute Finance's fiscal plan, which it then conveys to the Cabinet Committee on Priorities and Planning (P&P).

"Ops" and "Chops" also provided information on an ongoing basis to P&P. All proposals for new spending had to go through "ops and chops", and the Expenditure Review Committee also had a continuing role in examining existing programs to determine the possibilities for cost savings.

The foregoing demonstrates that between 1984 and 1989 the Conservative government became more committed to expenditure control and this responsibility was placed in the hands of the Minister of Finance and is well reflected in the evolution of the Expenditure Control Plan discussed below. The changes depicted strong political commitment to expenditure control which was most clearly revealed in the February 1992 budget also discussed below.

4.2 The Realignment of the Roles of the Central Agencies in Expenditure Management in the 1990's

The Task Force, PS 2000: The Renewal of the Public Service in Canada, addressed the issue of the realignment of the roles of the central agencies. The Lambert Commission had suggested that the roles of the Department of Finance and the Treasury Board should be elevated. Since that time both Finance and Treasury Board have enhanced their roles in the expenditure management process. However, there has been an associated effort to decentralize responsibility to departments depicted by the endorsement of Increased Ministerial Authority and Accountability (IMAA) and the new system of Operating Budgets. Consequently, several new management initiatives were adopted between the 1980's and the 1990's. This was most clearly reflected in the abandonment of the Policy and Expenditure Management System. The PS 2000 Task Force reaffirmed these issues and they were subsequently addressed in Bill C-26 (the Public Service Reform Act). Ian Clark, the Secretary of the Treasury Board, has indicated that the Board's Secretariat is more concerned with policy leadership than with administrative control. Consequently, the budgeting system became more adaptive in the 1990's. It appears that there is a more centralized planning system which is supported by a more decentralized system for purposes of implementation.

CHART 7

SOURCE: The Ottawa Citizen, February 4, 1989.

4.3 The Expenditure Control Plan, 1990-1991

The budgets and the expenditure plans between 1990 and 1992 were made under the new expenditure management system adopted in 1989. The deficit reduction strategy, the expenditure control plan and the endorsement of new management initiatives are indicative of the approach to expenditure management for the 1990's.

The 1990-91 Expenditure Plan (Table 2) was designed to result in fiscal savings of $19,495 million over the five years between 1990 and 1995. It was designed to limit growth in government spending while providing funding for key programs vital to Canadians. Program spending for 1990-91 was expected to grow by 3 percent. This was below the annual average growth rate of over 13 percent in the early 1980's. The planned rate of growth in program spending was less than the projected rate of inflation of 4.7 percent as measured by the Consumer Price Index (CPI).

TABLE 2

Consequently, program expenditures were expected to be reduced by 16 percent in real terms. The projected decline was due to the introduction of the Expenditure Control Plan which had five elements:

1) Exempting from reduction major federal transfers to persons and two transfers to the fiscally weaker provinces - equalization payments and payments made under the Canada Assistance Plan;
2) Limiting the annual growth rate of selected programs;
3) Freezing several programs in an effort to bring their plans into line with overall affordability;
4) Reducing or eliminating other programs in recognition of the government's serious fiscal problem; and
5) Launching new management initiatives to achieve more efficient and effective government operations.

The Expenditure Plan included a management strategy which encompassed ten key areas:

1) managing cash;
2) managing holdings;
3) managing assets;
4) implementing cost recovery;
5) improved organizational practices;
6) investing in automation;
7) streamlining regulations;
8) reducing paper burden;
9) using environmentally smart management practices; and
10) managing crown corporations.

The new initiatives adopted in 1990 included efforts to deliver programs differently. Accordingly, initiatives were taken to turn over programs to the private sector - (Consumer Affairs and Veteran Affairs). Special Operating Agencies were established through agreements between the Treasury Board and the departments. By way of illustration, the Passport Office and the

Public Service Staff Training Program were isolated as unique programs for such treatment.

The 1991-92 Expenditure Plan made allowance for $159 billion in spending, an increase of 5.1 percent over 1990-91. The extension of the Expenditure Control Plan was expected to result in savings of $14.8 billion over the subsequent five years. The savings for 1991-92 was estimated at $1.2 billion, $1.1 billion planned spending and $110 million related to cash management, privatization and other revenue-raising initiatives.

4.4 The Extension of the Expenditure Control Plan and Legislated Spending Limits

The February 1991 budget extended the Expenditure Control Plan introduced in the February 1990 budget. The plan projected a budget with financial requirements in surplus beyond 1993-94. It continued to exempt major social transfers and certain major transfers to provinces. The ceiling of 5 per cent per year growth on Canada Assistance Plan transfers to non-equalization receiving provinces was extended through 1994-95. Established Program Financing Transfers to the Provinces were frozen in per capita terms through 1994-95 and thereafter constrained to the rate of growth of GNP less three percentage points. Program spending was tightly constrained and significant reductions in the costs of government operations were announced. The 1991 budget measures, together with the associated public debt charges, were estimated to save $1.2 billion in 1991-92, and $2.3 billion in 1992-93. Cumulative savings over the 1991-92 to 1995-96 period were estimated to total almost $15 billion.

The government's commitment to expenditure restraint and deficit reduction was reinforced in the budget by the announcement of the government's intention to introduce legislated spending limits (Spending Control Act) and to establish a Debt Servicing and Reduction Fund. These could be viewed as an effort by Finance Minister Michael Wilson to make sure that the government remained committed to his expenditure restraint and deficit reduction agenda after he stepped down as Finance Minister.

Under the legislation mandating the limits, spending was to be constrained to an average of 3 per cent per year from 1991 to the end of 1995-96. This legislation was to establish upper boundaries on program spending. The limits would provide some flexibility to reallocate spending between years, but cumulative spending could not exceed the limits so that if spending was greater than the limits in one year it would have to be made up in later years. Spending resulting from some contingencies such as natural disasters or wars would be exempt as would expenditures on programs financed through premiums.

The legislated spending limits were bolstered by public sector wage restraint. The government announced that it was unwilling to contemplate public sector wage settlements in excess of 3 per cent over the next three years. In response to a public service strike, the government subsequently introduced legislation mandating wage increases of 0 and 3 per cent over the next 24 months.

The legislated spending limits and public sector wage guidelines formed an important part of the government's larger macroeconomic strategy of establishing the path to price stability and putting the country back on the track of strong sustainable growth. In the budget, the Minister of Finance announced with the Governor of the Bank of Canada the establishment of inflation targets of 3 per cent by the end of 1992, 2 1/2 per cent by the middle of 1994, and 2 per cent by the end of 1995. This was an important initiative to clarify the meaning of the Governor's commitment to price stability and to better coordinate monetary and fiscal policy.

The Debt Servicing and Reduction Fund is a special purpose account to which will be credited GST revenues and from which will be debited public debt charges (and gifts to the Crown earmarked for deficit reduction and proceeds from privatization). This fund was intended to allay public concerns about the GST and to give an institutional expression to the Prime Minister's commitment that any above-projected revenues from the GST would make a contribution to deficit reduction rather than be used to finance increased government spending.

4.5 Expenditure Planning in the February 1992 Budget

The February 1992 budget was the first budget of the new Finance Minster Don Mazankowski and the first Conservative budget since 1984 that was not brought down by Michael Wilson who will go down as the longest serving finance minister of the post-war period. While the budget continued to pursue the overriding objectives of expenditure restraint and deficit reduction, it involved some distinctive departures with regard to process, style and substance.

On the process side, the budget expenditure plan was put together without the participation of the Expenditure Review Committee. Even though the ERC was not formally abolished until January 1993, it never again played the key role it had in the 1990 budget in the preparation of the Expenditure Control Plan. There were several factors that led to the eclipse of the ERC and its ultimate demise. First, the ERC had not been very successful in the 1991 budgeting round in identifying government cuts and at the end of the day the task had to be carried out by the Minister of Finance. Second, the ERC effort had been very time consuming for all the participants. Third, many Ministers felt uncomfortable with the ERC as a forum for examining their programs.

The process followed for the 1992 budget was more informal than the one carried out under the Expenditure Review Committee. It depended very much on the personality of the new Finance Minister Don Mazankowski and his status as Deputy Prime Minister. Before becoming Finance Minister he had been Chairman of the Expenditure Review Committee. His successor was Gilles Loiselle the President of the Treasury Board and the Minister of State for Finance. The close personal relations between the Finance Minster and the President of the Treasury Board facilitated the preparation of the expenditure budget. They dealt bilaterally with departments to achieve expenditure restraint rather than through the Expenditure Review Committee. The close relations between the Finance Minister and the Prime Minister and the high status of the Finance Minister within the government as Deputy Prime Minister also facilitated the process. The key decisions on the government's expenditure budget would be agreed on between the Finance Minister and the Prime Minister and then ratified at a meeting of the Operations Committee followed by a meeting of the Priorities and Planning Committee. This process works well for the current Finance Minister. A different less centralized process would probably be required under another Finance Minister. This suggests that personalities play important roles in the process. The budget process has exhibited a continuous tendency to adapt to the leadership styles of the key participants.

Another change of process in the 1992 budget was the release of a statement by the Minister of Finance on Canada's economic and fiscal outlook in January a month before the budget. This gave the public useful information that helped to focus the pre-budget consultations which were more extensive than usual and even involved First Minister's Meetings on the economy. This suggests that there has been some opening-up of the budgetary process which has been a concern of all Finance ministers since the early 1960's.

In terms of substance, the budget extended and broadened the Expenditure Control Plan (Table 3). It continued to exempt from restraint some high priority areas such as major social transfers and certain major transfers to provinces. But departmental non-wage operating budgets were reduced from 1992-93 through 1996-97 by 3 per cent in each year. Significant initiatives were introduced to streamline the operations of government and forty-six government entities were eliminated, merged or privatized to lower costs and rationalize functions. The Expenditure Control Plan measures in the budget were estimated to yield savings of $1.1 billion in 1992-93 and $1.2 billion in 1993-94, with a five year cumulative savings of $7.3 billion.

While the budget continued to pursue the government's objectives of expenditure restraint and deficit reduction, it was more political and hence more popular than earlier Conservative budgets. In particular, for the first time since the 1988 tax reform it introduced significant tax reductions. These included a reduction in the personal income surtax, a proposal for restructuring child benefits, a Home Buyers Plan, and measures to enhance the competitiveness of manufacturing. The tax cuts were financed through expenditure reductions. Expenditure restraint has more political support if it is accompanied by tax cuts than if it is directed towards lowering the deficit. These initiatives demonstrate that the politics of expenditure management should not be underestimated. Budget reform procedures must accommodate political realities.

The adoption of the Policy and Expenditure Management System, the establishment of the Nielsen Task Force, the creation of the Expenditure Review Committee, the endorsement of New Management Initiatives, and the promulgation of legislated spending limits and inflation targets are the key developments between the 1980's and the 1990's that shaped the expenditure management system presently in operation. Together they comprise a concerted effort to reform the public expenditure management system over the course of the 1980's and into the 1990's. The commitment to expenditure restraint had, at least in part, been reinforced by globalism and the need to improve our competitiveness.

TABLE 3

SOURCE: Minister of Finance, Budget Papers, February 25, 1992, p.81.

5. SELECTED ISSUES IN EXPENDITURE MANAGEMENT REFORM

5.1 Initiatives to Improve Management

Centralization and Decentralization Initiatives

In 1986, the Government of Canada launched Increased Ministerial Authority and Accountability - or IMAA - a systematic initiative designed to change the culture of the Public Service. IMAA is designed to give ministers and senior managers the increased authority and flexibility they need to deal with changing circumstances and to manage effectively while enhancing the accountability of ministers and senior managers for results. The system provides for the signing of Memoranda of Understanding (MOU) between the Treasury Board and departments establishing an accountability framework for the implementation of IMAA.

Another important initiative recently launched by the Prime Minister was PS2000, a Task Force to examine the future of the Public Service. PS2000 established a specific Task Force on Resource Management and Budget Controls. The Discussion Paper dated August 7th, 1990 entitled "Public Service 2000: Report of the Task Force on Resource Management and Budget Controls" emphasized the decentralization thrust of IMAA. Consequently, it concluded:

One of its key objectives is to reduce central

> administrative controls to give deputy ministers and managers greater freedom to manage, with clearer accountability for and proper focus on results. This initiative addresses not only resource management, the focus of this Report, but the broader range of management issues being faced by the public service now and in the future.[52]

The Task Force endorsed the principle of the Operating Budget Approach. Under this approach, person-year controls would be eliminated. Each department program would get a separate budget called the operating budget which would include salaries, operating expenditures and minor capital costs. Departments would have full flexibility to move funds amongst these various components to achieve the most effective and efficient use of resources in delivering their programs. The Task Force recommended that the government should eliminate person-year controls and adopt single operating budgets starting in the 1992-93 fiscal year to foster a more productive use of resources and to focus on the real cost of delivering government programs. The Minister of Finance moved to implement these recommendations in the February 1992 budget.

5.2 Operating Budgets

Operating Budgets include salaries and wages, operating expenditures and minor capital. Operating expenditures include utilities, materials, supplies and other goods and services. Minor capital includes expenditures on furnishings, machinery and equipment that are primarily administrative in nature.

The government announced that it would introduce Operating Budgets on a pilot project basis over two years. Full implementation, which includes the elimination of person-year controls, is set for April 1, 1993. The Public Accounts Committee in its seventh report has supported the discontinuation of Treasury Board person-year controls.

The key objective is to further a managerial culture in which managers look at the cost-effectiveness of their decisions; recognize that employees are both a valued resource and a significant investment; and focus on the long-term implications of their decisions.

Operating Budgets will:

- improve decision-making - managers will focus on the full cost of delivering individual programs and services, not just the number of person-years required;

- increase efficiency - managers will be able to take decisions on the mix of inputs. The decision process will take into account costs that are not included in managers' budgets, such as employee benefits and accommodation;

- increase accountability for efficiencies at all levels of the Public Service - managerial decision-making will focus on cost-effectiveness.

5.3 Capital Budgeting

The Federal government does not prepare a separate capital budget as do private firms. Assets and capital purchases are treated as current disbursements in the public accounts and are not capitalized and depreciated over their useful lives. This has lead some observers to criticize that the public accounts overestimate the federal government deficit and have led the government to neglect capital expenditures.[53] It can not be denied that in a period of expenditure restraint as it is easier to postpone capital spending than to cut spending on ongoing programs and that this could lead to an erosion of the national public sector infrastructure. While it is true that since 1984 federal government capital expenditures as measured by the national accounts have actually declined in current dollar terms falling from $2,511 million in 1984 to $2,374 million in 1990, it is also important to remember that the 1984 level was a record, having almost doubled over a two year period as a result of the Special Recovery Capital Projects initiated to counter the 1981-82 recession. Capital budgeting may be a useful addition to the federal government's toolkit of budgetary planning, but given the relatively small proportion of federal spending accounted for by capital spending (only about 1 1/2 per cent in 1990) its impact on the measured deficit would be fairly small (only about 10 per cent). Its main advantage would be the greater priority it would attach to capital expenditures as opposed to current expenditures when budgetary decisions are being made. This would make a contribution, albeit modest, to good expenditure management.

5.4 Public Accounts

Since 1984 the Federal government has made a number of important accounting changes in response to reservations expressed by the Auditor General. The most important of these were described in the fiscal plan document released with the May 1986 budget. They were: the consolidation of the Exchange Fund Account, the Unemployment Insurance Account, the Western Grain Stabilization Account and other similar non-budgetary accounts into budgetary accounts; the treatment of loans to developing countries as budgetary rather than non-budgetary to better reflect the concessionary aspects of these loans; and the introduction of technical changes in the accounting for the Oil Export Charge and for internal government transactions. These accounting changes substantially broaden the scope of transactions included in budgetary expenditures, revenues and the deficit and thus raise budgetary expenditures and revenues and make the reported budgetary deficit or surplus a much better indicator of changes in the governments liabilities and debt. Because all of the changes are internal to the government sector they have no impact on financial requirements.[54]

These changes in conjunction with subsequent less important changes enabled Auditor General Ken Dye to write in the 1989-90 public accounts, which were the last that he audited, that "In my opinion these financial statements present fairly the financial position of the Government of Canada at March 31, 1990."[55] This marked the first unqualified opinion of an Auditor General of the public accounts in many years. However, this felicitous state of affairs did not last long because in 1990-91 the new Auditor General, Denis Desautels, included three reservations concerning the government's financial statements in his first report:

> 1) the government had improperly accounted for the effect on short-term wage restraint on employee pensions and should have recorded the savings over the remaining service life of the employees;
>
> 2) the government should have taken the $1,250 million reduction in the value of Petro-Canada resulting from the sale of some shares on the government's books in 1990-91 and not gone back and reduced the value in the accounts for earlier years;
>
> 3) the government should have reduced the income tax collected on the behalf of the provinces in 1990-91 by some $500 million and increased its own income tax correspondingly to reflect more recent information on tax assessments.

These adjustments would result in an increase of $2 billion in the 1990-91 deficit and an increase in federal government liabilities of $800 million. In contrast the accumulated deficit at the beginning of 1990-91 would be decreased by $1.2 billion.[56] The Auditor General also expressed concern that the Federal government did not disclose acquired physical assets on hand and available for use at the end of the year and did not provide a comparison of actual results for the year with those originally forecast in the fiscal plan. In our view, the latter is not a serious criticism as such information is routinely provided in federal budgets.

For many years, public servants and accounting professionals have worked to develop Generally Accepted Accounting Principles (GAAP) for the federal public sector. In March 1981 a Public Sector Accounting and Auditing Committee (PSAAC) was established by the Canadian Institute of Chartered Accountants (CICA). By the end of March 1991, PSAAC had issued 6 statements on accounting principles and a research study on the recording and reporting of physical assets. While as yet no agreed upon set of standards for good accounting and reporting procedures have been established, much progress has been made in recent years. The application of sound accounting principles to develop reliable financial statements is a fundamental prerequisite of efficient expenditure management.

5.5 Reform of the Estimates

One important development of the 1980's has been the reform of the Main Estimates. They now contain three parts. Part I gives an overview of the Government Expenditure Plan; Part II presents the details of the Main Estimates; and Part III provide individual department and agency expenditure plans (for 1991-92 there were 87 separate volumes). The new estimates respond to criticisms of the earlier one volume estimates for not providing any overview information or enough detail on individual departments. However, criticisms of the estimates remain, and there is still scope for improvements.

The Auditor General in his 1987 report complained that while Part III of the Main Estimates improves the information provided to Parliament, he still found the Part III repetitive and hard to read, half the initiatives were not costed, and the reporting was not consistent from year to year. He also recommended that the performance information be improved.[57]

In our view, a problem with the Main Estimates generally and Part I in particular is that it is not fully consistent with the budget fiscal plan. This can be a source of confusion when estimates appear in the Main Estimates for programs or agencies that have been eliminated or do not appear for new programs or agencies that have been announced. This problem occurs because the Main Estimates usually have to go to press before the budget is finalized in order to meet the March 1 deadline required to obtain interim supply. There are two solutions to this problem. Either the budget could be introduced in early February rather than late as has recently been the case or the House rules regarding interim supply could be amended to give the Treasury Board to March 15 to table the Main Estimates.

5.6 Program Evaluation

Following the creation of the Office of the Comptroller General of Canada (OCG) in 1978, the government formalized the process of program evaluation and substantially increased the resources devoted to evaluation. The OCG was responsible for establishing the framework for program evaluation. In 1981 it issued two publications to guide departments and agencies in carrying out program evaluations. These are: Principles for the Evaluation of Programs and Guide on the Program Evaluation Function. From the point of view of an economist, these documents are unsatisfactory because they focus almost entirely on process to the exclusion of more fundamental tools such as cost-benefit analysis. Indeed in 1984 and 1985 when the Nielsen Task Force looked at program evaluations to help it with its tasks, it was very disappointed with what it found. The Nielsen Task Force reported in damning terms that:

> Many study teams found that routine program evaluations were generally useless and inadequate for the work of program review. Yet, guided and inspired by the Office of the Comptroller General, departments have put in

> place significant evaluation groups over the past years....
>
> Ignoring occasional special evaluations requested by Treasury Board, routine evaluations conducted by departmental officials undertaken for the department's deputy minister. By definition, therefore, they tend to be self-serving, even though the scheduling of these evaluations are subject to the approval of the Comptroller General. The fact that evaluations are subject to disclosure under Access to Information legislation tends to make them even less frank.
>
> As a result, there is a tendency for these evaluations not to question the fundamental rationale for the reviewed programs, but to concentrate on program impact and delivery. The basic question of whether these programs should exist at all, as posed by the study teams, is rarely raised at the departmental level. A further limit to departmental evaluations is their inability to examine cross-agency programs or similar programs in other departments.
>
> The Private Sector Advisory Committee did not debate the issue of a permanent central government function for program evaluation. However, past experiments in this regard have not proved promising. In addition to the Treasury Board Planning Branch (1970-1978), three other attempts at centralized program evaluation were ultimately discontinued.
>
> It may be concluded from these experiences that proper "zero-based" program evaluations are not a function of government. A number of alternatives have been put forward including parliamentary committees, research bureaus of opposition parties, etc. Alternatively, ad-hoc ministerial reviews conducted jointly by public servants and private sector specialists may be a more appropriate instrument to take periodic stock of the situation. Whatever improvements are possible, fundamental change is essential since the current focus of program evaluation on direct spending is too narrow to be truly comprehensive.[58]

Our personal experiences with program evaluation suggests that little has changed since 1986 and the main thrust of the observations of the Nielsen Task Force are still valid. It would be useful to take a harder look at program evaluation in the

Government of Canada. Efficiency and effectiveness in government is important for the competitiveness of the Canadian economy and requires solidly based program evaluation that asks fundamental questions.

6. CONCLUSIONS

We have reviewed the development of the expenditure management system from the 1960's to the beginning of the 1990's. Recurring themes have been decentralization versus centralization, and the impact of philosophy on the system. Prime Ministerial and ministerial leaderships have shaped the evolution of the system. Personalities have also played an important role as well as formalized versus informal approaches to decision-making. The study has also pointed to the importance of Prime Ministers in the reform of the Canadian budgeting system. The Prime Minister, the Minister of Finance and the President of the Treasury Board are three important players in the budgeting system. The roles which they perform are critical to the performance of budgeting.

The process has oscillated between centralization and decentralization. A decentralized planning system has tended to work better when the government sector was expanding and the main decisions facing government were which new initiatives to fund. In a time of retrenchment such as the present when the emphasis is on expenditure restraint and deficit reduction a centralized system becomes imperative. The creation of the Expenditure Review Committee in 1989 depicted a shift toward centralization. But the situation is even more complicated than this. At the same time as the overall management of the system became more centralized, it was necessary to decentralize other aspects of the system to allow departments and agencies to manage more efficiently with less. Key examples are IMAA and operating budgets. Consequently, the relationship between the degree of centralization and decentralization of the system is obviously not a univariate one.

The philosophy of government has also shaped the development of the expenditure management system. There have been periods when efforts have been made to reform government along the lines of business or to insert business management principles into government. The two most important cases in point are the Glassco Commission and the Nielsen Task Force. The Cabinet Committee system blossomed under the Cartesian approaches to government organization of Prime Minister Trudeau and the Cabinet Secretary Michael Pitfield. This culminated in the complexity of the Policy and Expenditure Management System (PEMS) which increased the number of actors in the budgetary process. The emphases on the market and on reducing the burden of government on the private sector through expenditure restraint and deficit reduction have characterized the present Conservative government of Prime Minister Mulroney and has resulted in a more streamlined expenditure management system. The philosophical position of the Conservative government was outlined in Agenda for Economic Renewal and an effort was made to follow a consistent strategy between 1984 and 1993. This was most evident in the budget speeches and in the expenditure plans presented to Parliament.

Personalities have influenced the development of the expenditure management system. The relationships between Finance Ministers and Prime Ministers and other members of Cabinet have also been important determinants of how the system operates. Reforms in the budgeting system must be consistent with the working of our parliamentary cabinet system of government. The various Auditor Generals have had an impact on the system, given the fact that they have stressed the importance of sound financial management and accountability principles. Indeed in many cases the system has changed to reflect the styles of key actors such as Michael Wilson and Donald Mazankowski. A good example of this is the current more informal approach to expenditure management based on agreement between the Finance Minister, Donald Mazankowski, the Prime Minister, Brian Mulroney, and on bilateral relations between the Finance Minister and the President of the Treasury Board on the one hand and the program ministers on the other.

In addition, the expenditure management system has responded to external factors. The economic setting between the 1980's and the 1990's is characterized by globalism and competitiveness. This requires that the government establish a priority on improving the efficiency of the Canadian economy and on reducing the burden of government so that Canadian firms can compete more effectively in the global environment. In such a climate, reforms must be directed less at the internal budgeting system and more at the effects of the process on the private sector. The expenditure budgets must improve the government's ability to exercise a tight control over its spending. They must build on the current system which has a proven record of expenditure restraint and they should not undermine it. This is reflected in the formulation of the expenditure control plan. The Minister of Finance is a key role player with respect to these initiatives.

An encouraging development in expenditure management is the current attempt to coordinate fiscal and monetary policy through the promulgation of legislated spending limits and inflation targets. The most important contribution that expenditure management can make to enhancing the international competitiveness of the Canadian economy is to be consistent with a macroeconomic framework directed at achieving the price stability that is so necessary for sustainable growth in output and employment.

A final observation that can be made, based on our review of the development of the expenditure management system, is that it is always in a state of flux. Flexibility and the ability to adapt to emerging situations are a prerequisite of a good expenditure management system. The system that works best for the government today will not necessarily be the best one for tomorrow. Consequently, the expenditure management system must be flexible and must respond to the changing environment.

The expenditure management system must be responsive to domestic and international requirements. Our review demonstrates that the Canadian expenditure management system has been a very adaptive one. This is most clearly reflected in the management initiatives introduced following Glassco report in 1962, in the subsequent endorsement of program budgeting which was used to rationalize the expansion in expenditures between the 1960's and the 1970's, in the introduction of PEMS in 1981 which was designed to integrate policy and expenditures, and in the introduction of the Expenditure Review Committee in 1989 with the objective of controlling spending in the 1990's. Each system was viewed as the answer to the problems facing government expenditure management when introduced, usually with much fanfare, but, each in turn, was eventually found to be lacking in the face of emerging developments and pressures. The current system can be expected to suffer a similar fate. In fact, in late 1992, the Conservative government abolished the Expenditure

Review Committee, demonstrating once again the ever changing budgetary process.

This study has demonstrated that financial management represents one dimension of several institutional forces which shape public sector decision-making. Public budgeting is an integral part of the governmental institutional process which must be carefully examined. Our study has pointed to the changing roles of key participants in the public budgeting system. The objectives of the system have shifted toward managing deficit reduction and achieving greater efficiency and competitiveness. This has led to changes in the process. The system has had to be constantly monitored and modified to deal with pressing and changing current problems.

FOOTNOTES

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