SENATE SÉNAT

CANADA

# REPORT ON THE *SUPPLEMENTARY ESTIMATES (B), 2010-2011*

## Standing Senate Committee on National Finance

**SEVENTH REPORT**

*Chair*
The Honourable Joseph A. Day

*Deputy Chair*
The Honourable Richard Neufeld

December 2010

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**REPORT ON THE**
***SUPPLEMENTARY ESTIMATES (B), 2010-2011***

The *Supplementary Estimates (B), 2010–2011* were tabled in Parliament on 4 November 2010 and were referred to the Standing Senate Committee on National Finance. The *Supplementary Estimates (B), 2010–2011* are the second Supplementary Estimates to be tabled in the fiscal year ending on 31 March 2011. Once this report has been tabled, the Estimates must then be approved by the Senate. The federal government may then introduce a supply bill authorizing the appropriations.

The committee held four meetings to review these Supplementary Estimates. On 23 November 2010, officials from the Treasury Board of Canada Secretariat, Wilma Vreeswijk, Assistant Secretary, Expenditure Management Sector; David Enns, Deputy Assistant Secretary, Expenditure Management Sector; Sally Thornton, Executive Director, Expenditure Operations and Estimates Division; and Marcia Santiago, Senior Director, Expenditure Operations and Estimates Division, appeared.

On 24 November 2010, officials from the Privy Council Office, Wayne Wouters, Clerk of the Privy Council and Secretary to the Cabinet; Patricia Hassard, Deputy Secretary to the Cabinet, Senior Personnel and Public Service Renewal; Marilyn MacPherson, Assistant Deputy Minister, Corporate Services; and from the Treasury Board of Canada Secretariat, Daphne Meredith, Chief Human Resources Officer, discussed these Supplementary Estimates with the committee.

On 30 November 2010, officials from the Department of Indian Affairs and Northern Development, Colleen Swords, Associate Deputy Minister and Susan MacGowan, Chief Financial Officer, appeared before the committee to discuss Indian and Northern Affairs Canada's appropriations requests in the *Supplementary Estimates (B), 2010-2011*. Additionally, officials from the Department of National Defence, Kevin Lindsey, Assistant Deputy Minister, Finance and Corporate Services; Maj.-Gen. Robert Bertrand, Director General, Financial Management and Col. Sean Friday, Deputy Chief of Staff, Plans and Strategy, Canada Command, discussed the department's appropriations requests.

Finally, on 1 December 2010, officials from Atomic Energy of Canada Limited (AECL), Hugh MacDiarmid, President and Chief Executive Officer and Kent Harris, Senior Vice-President and

Chief Financial Officer, discussed AECL's financial situation and explained the rationale for its appropriations requests. Additionally, the committee discussed the Canada Account with: Derek Layne, Vice-President and Chief Risk Officer, Export Development Canada; Michael Fine, Director General, International Trade Strategy and Portfolio Bureau and Julie Insley, Director, International Trade Portfolio Division, Foreign Affairs and International Trade Canada; Alison Tait, Director General, Auto and Transportation Issues, Automotive and Transportation Industries Branch, Industry Canada; Brigita Gravitis-Beck, Director General, Air Policy, Transport Canada; and Richard Botham, General Director, Economic Development and Corporate Finance Branch, Department of Finance Canada.

## Overview of the *Supplementary Estimates (B), 2010-2011*

### Planned Spending

In the Estimates documents, planned spending appears as budgetary and non-budgetary expenditures, and by voted and statutory expenditures.[1] As shown in Table 1, the *Supplementary Estimates (B), 2010–2011* total about $2.3 billion. The federal government is seeking Parliament's approval to spend about $4.4 billion in voted appropriations, while statutory expenditures are expected to decline by about $2.0 billion.

**Table 1 – Total *Supplementary Estimates (B), 2010–2011***
**($ millions)**

| | Budgetary | Non-Budgetary | Total |
|---|---|---|---|
| Voted Appropriations | 4,359.7 | – | 4,359.7 |
| Statutory Appropriations | -1,215.4 | -809.4 | -2,024.8 |
| **Total** | **3,144.3** | **-809.4** | **2,334.9** |

Source: *Supplementary Estimates (B), 2010–2011*, p. 8.

Total estimates to date for this fiscal year are $266.6 billion, including $261.6 billion under the *Main Estimates 2010–2011*, $1.9 billion under the *Supplementary Estimates (A), 2010–2011*, $3.1 billion under the *Supplementary Estimates (B), 2010–2011* and total adjustments of

1 **Budgetary spending** encompasses the cost of servicing the federal public debt, operating and capital expenditures, payments to federal Crown corporations, and transfer payments and subsidies to other levels of government, organizations or individuals. **Non-budgetary expenditures** (loans, investments and advances) are outlays that represent changes in the composition of the federal government's financial assets. **Voted expenditures** are those for which parliamentary authority is sought through an appropriation bill. **Statutory expenditures** are those authorized by Parliament through enabling legislation; they are included in the Estimates documents for information purposes only.

$13.9 million. After adjustments, total budgeted expenditures for 2010–2011 are $280.5 billion. These expenditures are consistent with the total expenses of $277.8 billion established in the federal government's October 2010 *Update of Economic and Fiscal Projections*[2] and identical to the total expenses in the 2010 federal budget of $280.5 billion.[3]

## Examination of the *Supplementary Estimates (B), 2010-2011*

During the examination of the *Supplementary Estimates (B), 2010-2011*, senators explored the federal government's rationale for voted expenditure authorization requests and the reason for changes to statutory appropriation levels for federal departments, agencies and corporations.

### A. Voted Appropriations

#### 1. Atomic Energy of Canada Limited

In the *Supplementary Estimates (B), 2010-2011*, Atomic Energy of Canada Limited (AECL) requested voted appropriations of $294.0 million to cover the costs associated with: continued isotope production; repair and restart of the National Research Universal reactor; wind down of the Dedicated Isotopes Facility; health, safety and environmental upgrades at the Chalk River Laboratories; development of new reactor technology; funding of the shortfall in reactor life extension projects; and other operational pressures.

When senators questioned AECL's ongoing financial problems, officials from the Treasury Board noted that the CANDU division of AECL had experienced delays in its refurbishment projects. Additionally, they highlighted the difficulties experienced by the LabCo division of AECL in its Chalk River investments. Moreover, officials indicated that AECL is "doing repairs and refurbishment at a number of sites including Point Lepreau, Bruce, Gentilly and Wolsong. The commercial operation is going through some refurbishment. Health and safety upgrades are being done in the laboratories, and National Research Universal (NRU) is being secured." They acknowledged that AECL is having cash-flow issues, which necessitated the contingency fund transfer of $100 million.

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2 Department of Finance, *Update of Economic and Fiscal Projections*, October 2010, p. 30, http://www.fin.gc.ca/ec2010/pdf/efp-pef-eng.pdf.

3 Department of Finance, *Budget 2010*, 4 March 2010, p. 175, http://www.budget.gc.ca/2010/pdf/budget-planbudgetaire-eng.pdf.

In their questioning, senators sought more details about the nature of the appropriations requests made by AECL. In response, representatives of AECL informed the committee that its funding requests were not intended to cover AECL's expenses for the whole fiscal year and indicated that further funds would be requested in *Supplementary Estimates (C), 2010-2011*. Senators also requested information about where the funds being requested would be spent. According to the representatives, a large proportion of these expenditures, about $30 million to $40 million, have been directed to the repair and restart of the National Research Universal (NRU) reactor. As well, $150 million to $200 million would be directed to finance a number of the nuclear reactor life-extension projects, including at Point Lepreau. AECL representatives shared that, other than these requested expenditures, it has been under strict expenditure controls.

Senators also questioned AECL about its fixed-price contracts to supply life-extension services to nuclear reactors. Representatives of AECL informed the committee that, with respect to life-extension services, AECL overestimated its preparedness and underestimated the technical demands associated with providing those services. They indicated that, as a consequence, while AECL had received the expected level of revenue from these life-extension projects, the costs exceeded its projections, resulting in a loss on those projects. According to the representatives, most of these fixed-price contract issues for life-extension projects have been addressed. More specifically, the contract with Bruce Power was renegotiated to mitigate AECL's potential losses and the Gentilly 2 contract with Hydro-Québec has a lower risk of loss than other life-extension projects for AECL.

AECL representatives asserted that, with the repair and restart of the NRU, the upgrade at Chalk River and these life-extension projects, AECL's costs have recently been relatively high. They indicated that these costs, and – by extension – the size of parliamentary appropriations to AECL, are expected to be much lower after these initiatives have been completed. Representatives of AECL also noted that they were precluded from finalizing major new contractual commitments during the organization's current restructuring. Some senators were concerned that this inability to conclude major new contractual commitments would decrease AECL's revenue and increase its appropriations requests from Parliament.

## 2. Canadian International Development Agency

In the *Supplementary Estimates (B), 2010-2011*, the Canadian International Development Agency requested total voted appropriations of approximately $265.8 million, including $173.5 million in foreign aid for maternal, newborn and child health programs in developing countries consistent with Canada's G8 commitments. These initiatives are designed to strengthen national health systems, improve nutrition, and enhance disease treatment and prevention.

In their appearance before the committee, the Treasury Board officials explained some of the details of these programs and noted that they would be delivered in three parts. The first part would improve health systems by training more health professionals and improving "access to adequately equipped local health centres." The second part would support the provision of medicines and vaccines to reduce maternal and infant mortality. The third part would provide nutritious food and supplements to save lives. They could not provide any details about which countries would receive funding from these commitments.

## 3. Department of Indian Affairs and Northern Development

In the *Supplementary Estimates (B), 2010-2011*, the Department of Indian Affairs and Northern Development requested total voted appropriations of approximately $833.6 million, the majority of which is attributable to two appropriations requests. The first appropriations request is for $308.0 million to pay for settlement of specific claims - those arising from the alleged non-fulfilment of treaty obligations or the improper administration of land or other assets. The second appropriations request is in relation to the cost of awards to claimants with respect to the Independent Assessment Process and Alternative Dispute Resolution procedure in the Indian Residential Settlement Agreement of 2006 regarding sexual abuse, physical abuse and other wrongful acts suffered at Indian residential schools. The amount and timing of these payments depend on the number of claimants and the average settlement amount.

Officials from the Department of Indian Affairs and Northern Development stated that the $308.0 million for specific claims settlements was a re-profiling of unspent appropriations from a previous year. Senators had questions about the nature of these claims, including when the alleged non-fulfilment of treaty obligations or the improper administration of land or other assets occurred, the potential total cost of these claims and the total number of outstanding claims. The departmental officials noted that some claims date to the 1800s. These claims are currently booked as a $5 billion contingent liability for the federal government. Lastly, the officials informed the committee that 848 of these claims have been concluded; 557 claims remain outstanding.

The second major appropriations request by the Department of Indian Affairs and Northern Development, of about $294.6 million, was an incremental funding increase above the initial fiscal framework for the Indian Residential Settlement Agreement. In 2006, funds were budgeted to pay awards under the the Alternative Dispute Resolution process and the Independent Assessment Process for serious physical and sexual abuse as part of the Indian Residential School Settlement Agreement. While total funds of $960 million were budgeted to be distributed equally over a six-year period for this process, the number and size of the awards have exceeded expectations. In the current fiscal year, compensation of approximately $455 million will be paid in respect of about 2,500 claims.

Officials from the Department of Indian Affairs and Northern Development noted that the department had requested $47.6 million for its Food Mail Program in the *Main Estimates, 2010-2011*. In these Supplementary Estimates, it requested an additional $10 million for this program; senators questioned the rationale for this additional request. The departmental officials responded that the program's expenses are demand-driven. It also indicated that the department expects the new food delivery program, Nutrition North, to be more cost-effective, with cost containment measures that would hopefully obviate the need for future Supplementary Estimate requests for this program.

Senators were also concerned that other federal departments are using the Department of Indian Affairs and Northern Development as a source of funds for their programs. Transfers of approximately $17.6 million had been made in the *Supplementary Estimates (B), 2010-2011* to a number of departments, including $12.1 million to Natural Resources Canada primarily for its First Nations Forestry Program and its contribution to the Arctic Research Infrastructure Fund, $80,000 to the Department of Fisheries and Oceans to finance an English River fish counting fence in Labrador, and $346,300 to the Departments of Fisheries and Oceans and Natural Resources for their contributions to the International Polar Year. Health Canada, Parks Canada and Environment Canada received $765,000, $763,344 and $448,175 respectively for their work with respect to the Arctic

Research Infrastructure Fund. Officials from the Department of Indian Affairs and Northern Development stated that these transfers are within its mandate and ongoing priorities.

### 4. Office of Infrastructure Canada

In the *Supplementary Estimates (B), 2010-2011,* the Office of Infrastructure Canada made total voted appropriations requests of about $719.3 million, including the following four major appropriations requests:

- **Municipal Rural Infrastructure Fund** – funds for small municipal water, waste treatment, cultural and recreational projects ($184.2 million).
- **Building Canada Fund** – funds for national and regional infrastructure, especially water and wastewater treatment, national highways, public transit and green energy ($166.5 million).
- **Canada Strategic Infrastructure Fund** – authorization for large-scale regional or federal infrastructure, including highways and railways, local transportation, tourism or urban development, water or sewage treatment, and broadband telecommunications ($162.3 million).
- **Gas Tax Fund** – authorization for environmentally sustainable municipal infrastructure projects (low emissions as well as clean air and water), such as public transit, drinking water, wastewater infrastructure, green energy, solid waste management, and local roads and bridges ($102.6 million).

Senators were interested in the expiration of the Infrastructure Stimulus Fund and asked whether any of the aforementioned programs would expire by 31 March 2011. Officials from the Treasury Board responded that none of these programs would expire by that date, and that the appropriations requests reflect re-profiling of existing work.

### 5. Department of National Defence

In the *Supplementary Estimates (B), 2010-2011*, the Department of National Defence made total voted appropriations requests of about $815.0 million, most of which is attributable to two requests.

The first funding appropriations request, of approximately $649.1 million, is primarily for the Canada First Defence Strategy to increase capabilities through several initiatives, including Strategic

Airlift (C-17s), Tactical Airlift (C-130Js), the Family of Land Combat Vehicles and Regular Forces, as well as to finance their operation and maintenance. Senators requested that the department provide a more detailed explanation of this appropriations request. Of the $649.1 million requested, the departmental officials indicated that it would be divided into two portions. The first portion of $302 million would be directed to the Canada First Defence Strategy’s four pillars. Of that $302 million, $23.8 million would be directed to expenditures related to training, infrastructure maintenance and new infrastructure construction; $52 million would be dedicated to increasing the size of the Canadian Forces, including training, recruitment and associated costs; $160 million would be direct to procurement and material acquisition, including spare parts; and $67 million would be directed to force generation, more specifically the calling-up and training of reservists. No discussion occurred regarding where the second portion of the $649.1 million appropriation, valued at approximately $347 million, would be allocated. The departmental officials also mentioned that a number of projects have experienced delays, the largest of which is the C-130 Hercules project replacement, valued at $116 million.

The second funding appropriations request, of approximately $112.9 million, was made by the Department of National Defence for major capital projects, such as the Tactical Airlift Capability Project, the Medium Heavy Lift Helicopter Project, six additional projects indicated in the 2005 and 2006 federal budgets, and 17 ongoing projects. This funding request reflects updated project schedules.

Senators asked for more details on the projects that would receive funding from the authorization request of about $112.9 million. Officials from the department informed the committee that, among other smaller projects, the appropriation would be spent on a number of projects, including kitchen renovations at the recruit intake centre in St. Jean, Quebec, consolidation of the School of Electrical and Mechanical Engineering as well as the Military Police Academy at Canadian Forces Base Borden, construction of new headquarters for Land Force Western Area, and expansion of health services facilities and modernization of facilities for Defence Research and Development Canada, both at Canadian Forces Base Valcartier.

Senators questioned how the Department of National Defence was able to save about $80.2 million in expenditures in these Supplementary Estimates. The departmental officials replied that these savings were linked to two cost-saving initiatives in the 2010 federal budget: the freeze on reimbursements for salary costs and restraints on departmental operating budgets.

Lastly, in response to questions from senators about the $13.5 million appropriations request for the 2010 Winter Olympics, officials from the Department of National Defence informed the committee that members of the Canadian Forces remained in the area after the Olympics and Paralympics, including into the current fiscal year. The request would finance salaries and the costs of cleaning up and restoring about 50 sites used by the Canadian Forces during the Olympics and Paralympics.

## B. Statutory Appropriations

### Canada Account

In the *Supplementary Estimates (B), 2010-2011*, Export Development Canada (EDC) – after receiving repayments from General Motors of Canada (GM) and Air Canada – made payments of about $1.1 billion to the Consolidated Revenue Fund from the Canada Account. The financial transactions with these companies were considered to be above EDC's risk threshold; as such, the transactions were made with federal contributions to the Canada Account. According to officials from the Treasury Board, repayments of the Canada Account are non-budgetary in nature.

Senators posed a number of specific questions about the Canada Account and the repayment, to which officials from the relevant federal institution responded. In their testimony, officials from the Department of Foreign Affairs and International Trade informed the committee that its $100 million loan to Air Canada was fully repaid after approximately one year. Officials from the EDC indicated that the interest rate on that loan was set on commercial terms, with an interest rate in excess of 10%. Furthermore, officials from the Department of Foreign Affairs and International Trade and EDC said that General Motors fully repaid its $1.1 billion loan, which had an interest rate of 5% above the Canadian Dealer Offered Rate (CDOR).[4] The loans to both General Motors and Air Canada were repaid ahead of schedule, with applicable fees for prepayment. Some senators were concerned that the rate of interest paid by Air Canada was higher than that paid by General Motors. According to officials from the Department of Foreign Affairs and International Trade, the Government of Canada

[4] "The Canadian Dealer Offered Rate, named CDOR, is the recognized benchmark index for bankers' acceptances with a term-to-maturity of one year or less." See: Montréal Exchange, *CDOR,* 2010, http://www.m-x.ca/marc_terme_bax_cdor_en.php#.

– with a two-thirds share – and the Government of Ontario – with a one-third share – had jointly acquired 4.5% of GM's preferred shares and 11.7% of the common shares when they converted loans made to General Motors into equity. Similarly, the Government of Canada and the Government of Ontario combined provided a $2.9 billion loan to Chrysler to be repaid by 2017. According to officials from Industry Canada, that loan, much like the loan to General Motors, also has an interest rate of 5% above the CDOR. Moreover, the Government of Canada and the Government of Ontario jointly own 2% of Chrysler.

According to officials from the Department of Finance, the Government of Canada has already sold 35 million GM shares at $33 per share, which generated gross proceeds of $1.15 billion. The federal government retains about 175 million GM shares. Officials from the Department of Finance informed the committee that the Government of Canada's shares of General Motors and Chrysler were held by Canada GEN and Canada CH Investment Corporation respectively, both non-agent federal Crown corporations under the Canada Development Investment Corporation. These non-agent federal Crown corporations are registered under the *Canadian Business Corporations Act.* Additionally, shares of Chrysler and General Motors are held in separate corporations because the equity transactions for each company are expected to be conducted separately and with different commercial partners.

## Other Areas Explored by the Committee

### A. Carry Forward Provisions

Senators had questions about the federal government's carry forward provisions. Officials from the Treasury Board informed the committee that the carry forward provisions were established in the mid-1990s to prevent increased spending at the end of a fiscal year, a phenomenon known as "March madness." The carry forward provisions may represent as much as 5% of a department's operating budget. According to officials from the Department of National Defence, because of the department's size and the potential fiscal impact from a large carry forward, its carry forward provision is 2.5% of both its operating and capital appropriations.

## B. Transfers

Senators were concerned that the information presented in the *Supplementary Estimates (B), 2010-2011* was often unclear. Senators had questions about apparent funding reductions; officials clarified that these reductions were realignments, whereby funds are allocated to another envelope or another federal department or agency better able to manage the project. For example, while there appeared to be a $16.5 million reduction in the Green Infrastructure Fund, officials from the Treasury Board noted that there was no reduction in funding; rather, the file was transferred from Infrastructure Canada to Natural Resources Canada under the Forest Industry Transformation Program.

Additionally, senators sought information about an apparent funding reduction to the Department of Foreign Affairs and International Trade of approximately $117 million. Officials from the Treasury Board clarified that there was no net effect on spending; the reduction in *contributions* was a realignment, since there was an equivalent increase in the department's *grants.*

## C. Budgeting

Following questions by senators, officials from the Privy Council Office explained that the federal government's budgeting is conducted in a manner designed to generate spending room for priorities within the government's spending constraints. According to them, each year the federal government reviews approximately 25% to 30% of direct public spending in an effort to identify savings. Moreover, each department is required to identify its lowest priority and its lowest-performing 5% of spending.