

THE BUDGETARY PROCESS

Supporting the Pre-election Report

A TRANSPARENT, STRINGENT, PRUDENT AND
FLEXIBLE BUDGETARY PLANNING EXERCISE



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The Budgetary Process Supporting the Pre-election Report

Ministère des Finances

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INTRODUCTION

In recent years, the government has undertaken numerous actions to define a budgetary process that responds to the needs and expectations of the public and parliamentarians.

— The pre-election report is the end result of the process the government set up to draft the Québec budget and quantify its financial framework.

The purpose of this section is to report on the initiatives undertaken to make drawing up the budget a transparent, rigorous, prudent and flexible exercise.

□ **Four characteristics**

The process Québec selected essentially features four characteristics.

■ **A transparency process**

The budgetary process must be transparent.

Quebecers and parliamentarians must have all of the information required to evaluate the government's budget orientations.

■ **A rigorous process**

The process must be rigorous.

The budgetary process must be based on proven practices to guarantee that the evaluations are rigorous.

■ **A prudence process**

The budgetary process must be prudent.

The financial framework is vulnerable to both internal and external shocks and all forecasts involve some uncertainty. The budgetary process must take such risks and uncertainties into consideration.

■ **A flexible process**

The budgetary process must be flexible.

The economic and social context changes constantly; the very nature of a democratic society requires the budgetary process to be adjustable so that it can adapt quickly to events and to the implementation of public policy choice.

Budgetary planning process

Budgetary planning

Budgetary planning makes it possible to situate the government's budget policy within a financial framework. It defines the actions to be taken over the short and medium term, particularly to ensure adequate funding for public services based on the government's and Quebecers' ability to pay, in compliance with the laws in effect, including the *Balanced Budget Act* and the *Act to reduce the debt and establish the Generations Fund*.

Evolving planning

Budget planning is open-ended. That is why it is regularly reviewed and amended to factor in changes that could affect the financial framework.

In Québec, the government's preferred budgetary planning practices are built on a multi-year approach so that policies can be framed over several years. This approach means that measures can be implemented progressively.

Sound management of medium-term risks

The government's multi-year management hinges on the sound management of medium-term risk. For example, the government evaluates the cost of renewing government programs to ascertain and manage the expenditure overruns that might occur in subsequent years.

Long-term projections

The government also creates long-term projections that extend beyond five years. Such projections make it possible for the government to make decisions about trends that could have repercussions on public finances.

Budget secrecy

The budgetary planning process is subject to budget secrecy until the day of the budget speech. The concept of budget secrecy is rooted in the British parliamentary system. It is primarily intended to keep people with advance knowledge of budget measures from capitalizing on them by reorganising their activities.

1. THE TRANSPARENCY OF THE BUDGETARY PROCESS

The primary expectation Quebecers and parliamentaries have for the budget process is transparency.

It is essential for Quebecers to have all of the information required to evaluate and judge the government's budgetary orientations.

- The budgetary orientations must be **documented and published**.
- The documents made available must provide a **complete, accessible and comprehensible** vision of the financial framework.
- The vision must also cover the documentation produced with respect to the **accountability process**.

1.1 Documentation that supports the government's budgetary policy

In the March 2018 Québec Economic Plan, the government made public a document describing the process to establish the financial framework and public documentation to support the budgetary cycle.¹

— In particular, the document outlines the documentation provided to Quebecers in support of budget policy, including that produced in conjunction with the process for fiscal monitoring and accountability.

In recent years, the budget documentation has been revised so as to present the information in logical order and make it more comprehensible to Quebecers.

□ The Budget Speech

In it, when tabling the Budget in the National Assembly, the Minister of Finance sets out the budget policy—the government's priorities and commitments—including the objectives that have been selected and the ways chosen to achieve them.

□ Budget plan

The budget plan—which has been called the Québec Economic Plan since March 2015—is the document containing the various information elements related to the priorities and orientations announced in the budget speech.

■ Economic and budgetary policy directions

The plan sets out the economic and budgetary orientations² for the five years following the budget speech, including the current budget year.

It includes the government's consolidated financial framework, the strategic choices and measures, the annual targets for the Québec Infrastructure Plan and the debt reduction targets.

In addition to those orientations, the government also provides information derived from comparing Québec's economic and financial situation with that of other provinces, data on the change in revenue and expenditure as a percentage of the economy, and explanations of the adjustments made from the previous budget.

¹ See *Budgetary Process and Documents: Public Financial Accountability* published as part of the March 2018 Québec Economic Plan.

² In March 2018, the economic and budgetary orientations were covered in Section A of the Québec Economic Plan.

■ Detailed consolidated financial framework

The Québec Economic Plan gives Quebecers and lawmakers the detailed consolidated financial framework for the three years following the budget speech, including the current budget year.³

The financial framework is called consolidated because it contains the data on all of the entities within the government reporting entity. In March 2018, the consolidated financial framework covered close to 350 different entities.

The detailed consolidated financial framework gives Quebecers and parliamentarians information on the factors affecting the changes in revenue and expenditure, and presents adjustments to the financial framework since the last budget was tabled.

The detailed consolidated financial framework is a direct source of management information for the entities within the government reporting entity; it helps them plan their short-term operations based on the financial resources that will be available to them.

■ Information to support budgetary policy

The Budget Plan, or the Québec Economic Plan, contains the information that supports budgetary policy, namely information that presents the government's orientations for economic development, its economic forecasts, and detailed information on the debt and federal transfers.

In particular, the information clustered under the theme of government orientations for economic development provides detailed information in plain language on the various tax and budgetary initiatives announced in the budget.⁴

The economic forecasts are in a special section due to the central role they play in forecasting revenue and expenditure.^{5,6}

³ The detailed financial framework is presented in Section F of the March 2018 Québec Economic Plan.

⁴ In the March 2018 Québec Economic Plan, the government's orientations for economic development are set out in Sections B, C and D. Section B summarizes all of the initiatives. Section C details the initiatives designed for individuals and the community. Section D describes the initiatives introduced to boost economic development.

⁵ See Section E of the March 2018 Québec Economic Plan.

⁶ The information that supports budgetary policy also includes a detailed forecast of the evolution of the debt and financing program over five years (Section G of the March 2018 Québec Economic Plan) and Québec's position with respect to federal transfers (Section H).

❑ Specific details and perspectives

Complementary to the Budget Speech, another series of documents includes publications that provide certain details or particular perspectives to Quebecers and parliamentarians.

- The government provides an entire array of additional information concerning, for example, things like legislation pertaining to budgetary balance and the Generations Fund,⁷ or other one-time information about some budget initiatives.⁸
- In particular, the procedural requirements respecting the tax measures are described in detail in the document entitled Additional Information.
- The government publishes brochures that are also part of budgetary documentation to highlight certain themes tackled in the budget.⁹

⁷ This category includes measures requiring an amendment to legislation, Québec's budgetary statistics and sensitivity analyses for economic and financial variables.

⁸ In March 2018, the government published further information on the *Tax Fairness Action Plan*, the cannabis framework and support for the taxi industry.

⁹ This series of documents also includes the economic and financial summary and calculators available on the Ministère des Finances website, as well as the executive summary of the budget.

1.2 Complete, accessible, plain-language documentation

The government has done many things to enhance the transparency of budget documents in recent years.

The transparency compares favourably to the transparency of budget documents available in other Canadian provinces in many respects.

☐ Complete documentation

The budget documentation provides complete information on the data presented and assumptions used.

■ Complete financial framework

The information presented in the budget documents is complete and accessible to everyone. It describes changes to the financial framework's components and its revisions. In the same way, the assumptions are explained clearly and justified so that the reader grasps the changes made since the last budget.

For example, the Ministère des Finances releases a range of information, such as:

- economic and financial indicators that explain revenues and expenditures;
- growth rates and adjustments to the main components of the financial framework;
- government orientations and announcements that have an influence over the forecasts;
- the impact of economic conditions and government orientations on the budget situation and, if applicable, major changes in public services;
- comparisons with other Canadian provinces.

■ Economic forecasts

The economic forecasts used by the government play a critical role in projecting revenue and expenditure, as well as managing the debt and defining economic policies.

The budget documents provide extensive information on those forecasts, including the forecast change in Québec's primary economic variables over two years, the growth outlook for both real and nominal GDP over five years, the expected progress of the Canadian economy, U.S. economy and world economy, and the evolution of a variety of financial market variables.

■ **Federal transfers**

The section on federal transfers sets out the forecast for federal transfer revenues, which are federal government revenues paid to Québec under the *Federal-Provincial Fiscal Arrangements Act*, to which revenue from other programs is added. It also sets out Québec's requests to the federal government.

The information on federal transfers informs Quebecers about Québec's requests. The section is also addressed to the other provinces and the federal government, giving them Québec's perspective on the transfers.

■ **Medium-term projections**

The Ministère des Finances also regularly publishes medium-term projections on the development of the economy, Québec's financial framework and debt.

□ **Accessible documentation**

The budget documents are presented in an understandable way and their structure makes the information easy to access.

■ **Presentation of the Québec Economic Plan**

The sections of the Québec Economic Plan devoted to various fiscal and budgetary initiatives illustrate the concern with accessibility.

All government initiatives are categorized by theme, and the document spells out their financial impact, how they will be funded, and the context for the government measures. The terms for applying tax measures are also described in detail in the additional information.

That gives all Quebecers an exhaustive statement of the fiscal and budgetary initiatives announced in the budget, together with explanations about them and the reasons why they were adopted. Details of the measures and specific terms of application are released after the budget is tabled. The minister responsible for each measure handles this task.

■ **Information presented systematically**

The array of information that makes it possible to understand all aspects of budget policy is made available to all Quebecers in a systematic way.

■ A strong effort compared with other Canadian provinces

The budget document presentation Québec has chosen is the most complete of any province in Canada.

- Québec is the only province that provides a detailed explanation of the adjustments to revenue and expenditure, and makes the connection between the changes and the economic situation as part of an economic and financial update.
- Québec is also the only province to produce a monthly report on its financial operations.

□ Plain-language information

With each budget, the government issues a summary that sets out all of the economic, financial and fiscal orientations in just a few pages.¹⁰

■ Budget papers

The budget papers included in the budget documentation are also intended to provide a plain-language explanation of certain orientations announced in the budget.

The budget papers provide complete information on the initiatives announced in the budget for specific issues; in-depth background information is often included.¹¹

■ Use of digital technology

The development of digital technology provided the government with an opportunity to present its information in plainer language.

All the different calculators and “Québec by the Numbers,” available on the Ministère des Finances website, give Quebecers understandable information and rapid access to the budget initiatives that directly concern them.

¹⁰ In March 2018, the document was called *Economic Plan in Brief*.

¹¹ The 2018-2019 budget documentation comprises thirteen papers that address topics such as health, education, climate change and disposable income.

1.3 Accountability

The government's desire for transparency cannot be limited to the budget period.

Fiscal and financial policy directions must be monitored and an accountability report drawn up, while making this information available to all Quebecers.

Three monitoring and accountability documents allow Quebecers to better understand the state of public finances throughout the budgetary cycle: the fall update, the monthly report on financial transactions and the public accounts.

☐ The fall update

The government has published a fall update every year since the 2006-2007 fiscal year. This publication presents the government's update on Québec's economic and financial situation over the course of the fiscal year.

As part of the fall update, the government may choose to announce new policy directions that will be restated when the upcoming budget is published.

The Québec government's fall update is the most comprehensive document of its type compared to other Canadian provinces.

☐ The monthly report on financial transactions

The government has also published a monthly report on financial transactions since the 2006-2007 fiscal year. Eleven times a year, Quebecers have access to an overall picture of the monthly progress when it comes to public finances.

☐ The public accounts

In accordance with the *Financial Administration Act*, the government tables its public accounts at the end of the budgetary cycle.

The document presents the government's financial statements and financial information pertaining to government departments, budget funded bodies and special funds, as well as other information including an analysis of financial indicators.

It should be noted that the Auditor General of Québec presents its opinion on the consolidated financial statements as part of its audit.

2. RIGOROUS BUDGETARY PROCESS

The various documents published at the same time as the annual budget and throughout the budgetary cycle are intended to ensure transparency in the budgetary process. The process must meet a second expectation on the part of Quebecers: it must be rigorous.

- It must be based on proven **practices** so as to guarantee that the evaluations and forecasts are rigorous.
- When it comes to forecasts, their rigorous nature may be measured by evaluating “**forecast performance**,” which is the difference between formulated forecasts and actual changes.

2.1 Practices used

The Québec government has gradually implemented a series of practices in order to ensure a rigorous budgetary process.

- The Ministère des Finances works closely with the departments and bodies of the Québec government. This collaboration hinges on precisely defining the responsibilities of everyone involved. The government also works very closely with the Secrétariat du Conseil du trésor.
- Very detailed forecasting models allow for precise simulation of the assumptions used.
- The Ministère des Finances bases its forecasts on the most recent economic and financial results.
- The process conforms to legal and regulatory provisions as well as public sector accounting policies.

These practices are implemented for the various budget forecasting exercises that determine the financial framework and debt valuation: economic forecasts, revenue forecasts, expenditure forecasts, including financing needs forecasts to determine the debt level.

❑ **Economic forecasts**

Economic forecasts are made in advance of the process that determines the financial framework and debt. They serve as inputs for revenue and expenditure forecasts. They indicate the anticipated movement of the Québec economy, the economy of Québec's main trading partners, the financial markets, the price of raw materials and the global economy.

The Ministère des Finances goes to great lengths to ensure that each step follows best practices.

■ **Tracking changes in the economic situation**

During the initial step, the Ministère des Finances tracks changes in the economic situation, gathers and processes the most recent official statistics and analyzes factors that could influence forecasts.

■ **Economic forecasting models**

During the second stage, the Ministère des Finances uses economic forecasting models to produce consistent forecast scenarios. These very detailed forecasting models allow for reflection on the assumptions used.

■ **Results analysis**

During the third stage, the results are analyzed.

Certain parameters and assumptions are re-evaluated in order to come up with consistent, reliable forecasts. For example, the economic forecasts may be adjusted so as to reflect the impact of major budgetary measures on economic growth.

This stage also includes the cross validation of assumptions used with private sector forecasts. The comparison with private sector forecasts helps determine the plausibility of the assumptions as well as the risks that could influence results.

❑ Revenue forecasts

Revenue forecasts are drawn up once economic forecasts have been finalized as they are based, in part, on the latter. Revenue forecasts also depend on the government's fiscal policy directions.

Revenue forecasts are based on two distinct processes involving either own-source revenues or federal transfers.

■ Own-source revenue

In the case of own-source revenue,¹² the forecasts result from concerted action by several stakeholders, in particular the Ministère des Finances, government departments and bodies and government enterprises. The revenue of each source is determined separately using a forecasting method and models established specifically for the source.

■ Ongoing analysis

The information required for creating forecasts is repeatedly compiled and analyzed throughout the year. For the most part, this information comes from reports produced by Revenu Québec and by the Comptroller of Finance.¹³

Thanks to these reports, the Ministère des Finances can carry out in depth analyses of the changes in revenue sources and their components, thus reducing the risks associated with forecasting.

Forecasts of revenue from government enterprises is determined according to information that the latter submit, namely their earnings forecasts and the information on which the forecasts are based.

■ Using models

All the data and information is processed using models that are designed for each source of revenue.

These models facilitate the production of a detailed revenue forecast broken down into components in a manner that captures the behaviour of economic agents, thus allowing for more efficient monitoring throughout the year. As part of a continuous improvement process, these models are updated regularly to ensure the reliability of the forecast.

¹² In 2018-2019, own-source revenue represents 78.6% of the government's total revenue.

¹³ The compiled information used to forecast own-source revenue also comes from the Institut de la statistique du Québec, Statistics Canada, various government departments, public bodies and government enterprises.

■ Controls and validations

Throughout the own-source revenue forecasting process, controls and validations are carried out to ensure the accuracy and relevance of the assumptions used.

■ Integration of new fiscal and budgetary measures

Once the forecasts have been established, the Ministère des Finances incorporates new fiscal and budgetary measures that will impact revenue into the financial framework.

■ Federal transfers

When it comes to federal transfers,¹⁴ the forecasting process primarily consists in collecting and analyzing a range of economic, demographic and fiscal data.

The revenue forecast from the Canada Health Transfer, the Canada Social Transfer and equalization is established using a model that precisely reproduces the parameters outlined in the *Federal-Provincial Fiscal Arrangements Act*.

The forecast of revenue from other programs is determined based on inputs from various government departments and federal bodies.

The Ministère des Finances also uses as inputs several variables from the previously established economic forecast.

When it comes to federal transfers, controls and validations are carried out during the forecasting process to ensure the accuracy and relevance of the assumptions used, especially those of an economic nature.

¹⁴ In 2018-2019, federal transfers represent 21.4% of the government's total revenue.

❑ Expenditure forecasts

As is the case with revenue forecasts, expenditure forecasts are carried out once economic forecasts have been finalized as they are based, in part, on the latter. Expenditure forecasts are also based on the government's fiscal policy directions.

Expenditure forecasts are established using two different processes, depending on whether the expenditure is a mission expenditure or debt service expenditure.

■ Mission expenditures

Mission expenditure forecasts¹⁵ are established by the Ministère des Finances in close collaboration with the Secrétariat du Conseil du trésor and all government departments and public bodies. The Ministère des Finances collaborates closely with the Secrétariat du Conseil du trésor and the responsibilities of each department are outlined in the legislation.¹⁶

The process established to determine the forecasts is made up of five steps, which are clearly defined.

■ Clear and detailed instructions

Clear and detailed instructions are communicated to government departments, public bodies and other government reporting entities. This step is vital in guaranteeing the quality of forecasts and the rigorous nature of the completed work.

The instructions communicated include the economic and budgetary parameters that must be taken into account. It is essential that the same assumptions be used to ensure that government program renewal costs are coherently evaluated by the various government departments and bodies.

■ Multi-year spending target

The Ministère des Finances determines the multi-year spending target.

This target is determined based on the government's fiscal policy directions and its capacity to pay, which stems, in particular, from the changes in government program renewal costs, revenue and expenditure during the year.

¹⁵ In 2018-2019, mission expenditures represent 91.5% of the government's total expenditure.

¹⁶ *Act respecting the Ministère des Finances and Public Administration Act.*

■ Government program renewal costs

At the same time, the Secrétariat du Conseil du trésor, in collaboration with government departments and public bodies, estimates the renewal costs of government department programs and other mission expenditures.

— “Government program renewal costs” entail an exhaustive evaluation of the costs associated with the renewal of service delivery and existing programs.

The estimate considers the relevant economic, demographic and salary parameters, such as changes in the price of goods and services or changes in the clientele. The estimate of program renewal costs also incorporates the impact of government decisions, for example the cost of collective agreements or the cost of new measures.

■ Managing the differences observed

The multi-year target is compared with government program renewal costs for the possible management of the differences observed, whether they display a surplus or a deficit in relation to program renewal costs.

■ Total mission expenditures

During the final stage of this process, the Ministère des Finances establishes the total mission expenditures.

— Furthermore, based on the evaluation of program renewal costs, the Secrétariat du Conseil du trésor determines the government departments' and bodies' appropriations for the budget's reference year as well as the expenditure budget for special funds and non-budget-funded bodies.

The new tax and budget measures that affect expenditure are then incorporated into the forecasts.

■ Debt service

The direct debt service forecast¹⁷ is obtained using a model that takes into account the characteristics of each financial instrument that makes up the debt. The forecast uses the most recent actual results as a base. It factors in all of the government's decisions that impact financing needs.

The direct debt service forecast integrates the debt management strategy implemented by the government.

The debt service forecast also includes interest on liabilities with regard to pension plans and future employee benefits.

¹⁷ In 2018-2019, the debt service represents 8.5% of the government's total expenditure.

❑ **Reconciliation of forecasts and policy directions**

Once revenue and expenditure forecasts have been created, the next step involves reconciliation of the government's forecasts and policy directions.

This reconciliation is carried out in three phases.

■ **Overview of the budgetary situation**

During the first stage, the profile of the fiscal position is prepared when the revenue and expenditure forecasts are pooled. A complete representation is obtained through the consolidation of the forecasts produced by the Ministère des Finances and by those produced by government departments and bodies.

■ **The government's policy directions**

During the second stage, the government determines its economic, fiscal, budgetary and financial directions.

These directions are primarily based on pre-budget consultations and on requests submitted by government departments and public bodies. Some of these proposals are subject to in-depth analyses, including alternate scenarios.

It is incumbent upon the government to choose the policies and measures that will be integrated into budgetary policy. The initiatives are adopted especially according to the government's priorities and the leeway achieved during the financial framework elaboration process.

■ **Validating the consistency of the financial framework**

During the third stage, the Ministère des Finances validates the consistency of the financial framework in light of the measures adopted and the government's policy directions. This final analysis ensures that the assumptions, forecasts and policy directions used are plausible.

2.2 Accuracy of achieved results: forecast performance

In order to evaluate the accuracy of achieved results, the Ministère des Finances compares its forecasts with the results observed.

This forecast performance measure is applied to economic, own-source revenue and mission expenditure forecasts.

❑ Economic forecast performance

The performance of economic forecasts in relation to achieved results is a vital step. Economic forecasts are the starting point for establishing the financial framework.

■ Most likely outlooks

The economic forecasts must correspond to the most probable outlooks at the time they are created, based on the information available at that time.

— The forecasts must take risks into account.

The economic forecasts must be centred and lead to an accurate revenue forecast. A large gap would translate into inadequate decisions in terms of government policies.

— The likelihood of forecasts is evaluated by comparing the Ministère des Finances forecasts to those of private sector institutions.

■ The most accurate outlooks after the fact

The quality of forecasts may also be evaluated by comparing them ex post to what has transpired—the facts can only be evaluated in hindsight.

— When it comes to economic forecasts, the facts can only be quantified a few years after the period in question.

The comparison between forecasts and subsequent official data constitutes a forecast performance measure.

■ An initial evaluation while drawing up forecasts

When being drawn up, economic forecasts are compared to private sector forecasts.

— This comparison allows the Ministère des Finances to undertake an initial assessment of changes in the economic situation.

The Ministère des Finances reviews forecasts drawn up by eleven private sector institutions.¹⁸

Overall, since 2002, the economic forecasts of the Ministère des Finances have been comparable to the average private sector forecasts. These forecasts are between the lower and higher limits of the private sector forecasts.

TABLE 1

Québec real GDP initial forecast: comparison with the private sector (percentage change)

	Ministère des Finances du Québec ⁽¹⁾	Private sector ⁽²⁾		
		Low	Average	High
2002	1.7	0.4	1.3	1.7
2003	2.5	2.0	2.9	3.4
2004	2.7	2.2	2.6	3.0
2005	2.4	2.1	2.4	2.8
2006	2.5	1.9	2.5	2.7
2007	1.8	1.1	1.8	2.4
2008	1.5	0.9	1.6	2.4
2009	-1.2	-2.5	-1.2	-0.4
2010	2.3	2.0	2.4	2.8
2011	2.0	1.8	2.2	2.6
2012	1.5	1.4	1.6	2.0
2013	1.5	1.3	1.5	1.7
2014	1.8	1.5	1.8	1.9
2015	2.0	1.7	2.0	2.4
2016	1.5	1.3	1.6	2.0
2017	1.7	1.5	1.7	1.9

(1) For example, the 2002 forecast was published in Budget 2002-2003.

(2) Ministère des Finances du Québec summary, which contains the forecasts of 10 private sector institutions for 2002 to 2014 and 11 institutions for 2015 to date.

Sources: Institut de la statistique du Québec, Statistics Canada and Ministère des Finances du Québec.

¹⁸ The 11 private sector institutions whose economic forecasts are reviewed by the Ministère des Finances are the Laurentian Bank of Canada, Royal Bank of Canada, Scotiabank, TD Bank, BMO Capital Markets, CIBC World Markets, Conference Board of Canada, Desjardins, National Bank Financial, IHS Markit and Industrial Alliance.

■ Retroactive analysis of economic forecasts

The retroactive analysis of the differences in economic forecasts compared to observed results allows the Ministère des Finances to determine the accuracy of the achieved results and thus the efficiency of the forecasting process.

■ Retroactive analysis

This retroactive analysis can only be carried out after the fact as official statistics on the state of the economy are subject to a series of revisions.

When it comes to real GDP, final statistics for a given year are generally published after several revisions. They generally stabilize after three annual revisions.

- For example, the first estimate for the 2013 real GDP was published by statistical agencies in March 2014. This data was subsequently revised in November 2014 and again in 2015 and 2016.
- Thus, the 2013 real GDP growth increased from 1.0% to 1.4% between the first forecast and the last available estimate to date.¹⁹
- Furthermore, Statistics Canada may modify these statistics over the coming years while drawing up broader historical forecasts. These revisions in particular aim to improve forecasting methods or modify certain concepts.

¹⁹ For more information, see page 65 of *Budgetary Process and Documents: Public Financial Accountability* published as part of the March 2018 Québec Economic Plan.

■ Differences in official data observed ex post

The Ministère des Finances carried out a retroactive analysis of the differences observed between the first estimated observation for a given year—which was used to draw up the financial framework of the same year—and the first and last official data published by statistics agencies.

Between 2002 and 2016, the differences between the forecasts of the Ministère des Finances and the first estimate of official data are positive for certain years and negative for others, indicating that the forecasts do not include a systematic bias. This represents, on average, a difference of 0.1 percentage point for the entire period, which indicates a low bias. The standard deviation, which represents the deviation dispersion, is 0.9 percentage point. The lower the standard deviation, the more precise the forecast.

When comparing the forecasts of the Ministère des Finances with the final observed data, a mean deviation of 0.2 percentage point is observed for the entire period.

TABLE 2

Québec real GDP forecast: comparison with observed data

(variation in percentages and difference between the forecast and observed date in percentage points)

	Initial forecast of the Ministère des Finances du Québec ⁽¹⁾	First estimated observation		Latest estimated observation available	
		Observed data	Difference	Observed data	Difference
2002	1.7	4.1	-2.4	2.9	-1.2
2003	2.5	1.7	0.8	1.2	1.3
2004	2.7	1.9	0.8	2.5	0.2
2005	2.4	2.1	0.3	1.5	0.9
2006	2.5	1.6	0.9	1.2	1.3
2007	1.8	2.5	-0.7	2.4	-0.6
2008	1.5	1.0	0.5	1.9	-0.4
2009	-1.2	-1.4	0.2	-0.8	-0.4
2010	2.3	2.8	-0.5	2.0	0.3
2011	2.0	1.7	0.3	1.9	0.1
2012	1.5	1.0	0.5	1.0	0.5
2013	1.5	1.1	0.4	1.4	0.1
2014	1.8	1.3	0.5	1.8	0.0
2015	2.0	1.1	0.9	1.0	1.0
2016	1.5	2.0	-0.5	1.4	0.1
MEAN DEVIATION			0.1	0.2	
STANDARD DEVIATION			0.9	0.7	

(1) For example, the 2002 forecast was published in Budget 2002-2003.

Sources: Institut de la statistique du Québec, Statistics Canada and Ministère des Finances du Québec.

■ **Forecasts more comparable retroactively than those of the private sector**

In order to determine the accuracy of the forecasting work within the framework of the budgeting process, the Ministère des Finances compared the differences observed retroactively between the forecasts of the Ministère des Finances and the official data published by statistics agencies with the differences observed between the private sector forecasts and the same official data.

The initial forecasts of the Ministère des Finances are more comparable than the average private sector forecast.

- For the 2002-2016 period, the mean deviation is 0.2 percentage point for the average private sector forecast and 0.1 percentage point for the Ministère des Finances.
- The standard deviation for the 2002-2016 period is 1.0 percentage point for the private sector, compared to 0.9 percentage point for the Ministère des Finances.

When it comes to the comparison with the last available estimated observation, observations of the Ministère des Finances are, on average, comparable to private sector's forecasts.

- The mean deviation for the 2002-2016 period is 0.3 percentage point for the private sector and 0.2 percentage point for the Ministère des Finances.
- The standard deviation is 0.8 percentage point for the private sector and 0.7 percentage point for the Ministère des Finances.

TABLE 3

Difference between economic forecasts and official data from 2002 to 2016
(percentage points)

	First estimated observation		Latest estimated observation available	
	Ministère des Finances du Québec	Private sector average	Ministère des Finances du Québec	Private sector average
Mean deviation	0.1	0.2	0.2	0.3
Standard deviation	0.9	1.0	0.7	0.8

Sources: Institut de la statistique du Québec, Statistics Canada and Ministère des Finances du Québec.

❑ Own-source revenue forecast performance

The retroactive analysis of the differences in own-source revenue forecasts reveals a mean deviation of 0.3 percentage point in 2014-2015, 0.9 percentage point in 2015-2016 and 1.4 percentage point in 2016-2017.

On average, the difference is less than 1 percentage point for the three years. The larger difference in 2016-2017 is due to the elimination of the health contribution as of 2016, announced retroactively within the framework of the March 2017 Québec Economic Plan. Excluding this information, which was not available at the time the forecast was created, the difference is reduced to 0.8 percentage point.

TABLE 4

Changes in forecast and observed own-source revenue (as a percentage and in percentage points)

	2014-2015	2015-2016	2016-2017
Budget 2014-2015	3.9	3.5	3.6
March 2015 Québec Economic Plan		4.4	3.3
March 2016 Québec Economic Plan			2.6
Observed⁽¹⁾	3.6	4.9	1.8
Mean deviation⁽²⁾	0.3	0.9	1.4

(1) According to the public accounts in the reference year.

(2) Mean deviation, in absolute value, between the changes observed and forecast in the various budgets for the given year.

The analysis also included the three main components of own-source revenue: personal income tax, corporate taxes and Québec sales tax.

- The analysis showed that the forecasts were accurate given the low average forecasting differences. These forecasts are not biased as the observed differences were both higher and lower.
- The forecasts are more volatile for certain own-source revenue: corporate tax in particular, due to its high variability.

■ **The most precise economic forecasts for own-source revenue in Canada**

The economic forecasts for own-source revenue established by Québec and observed over a period of 15 years are the most precise in Canada.

According to the C.D. Howe Institute, Québec ranks first when the difference between forecast and observed data over the past 15 years is compared with the difference calculated by the provincial and federal governments.²⁰

TABLE 5

Standard deviation in forecasts for own-source revenue of provincial, territorial and federal governments from 2002-2003 to 2016-2017

	Deviation ⁽¹⁾ (%)	Rank
Québec	1.8	1
Federal government	2.0	2
Prince Edward Island	2.3	3
Manitoba	2.8	4
Nova Scotia	2.8	5
New Brunswick	3.1	6
Ontario	3.7	7
British Columbia	4.7	8
Northwest Territories	5.0	9
Yukon	5.3	10
Nunavut	6.7	11
Saskatchewan	10.9	12
Newfoundland and Labrador	11.5	13
Alberta	12.5	14

(1) The root-mean-square error is used to measure the deviation.

Sources: Ministère des Finances for Québec and the C.D. Howe Institute for the other governments.

²⁰

WILLIAM B. P. ROBSON, FARAH OMRAN, *Blown Budgets: Canada's Senior Governments Need Better Fiscal Controls*, Commentary No. 512, Toronto, C.D. Howe Institute, 2018, p. 8.

■ **Personal income tax**

Personal income tax is the government's largest source of revenue. In 2018-2019, revenue from personal income tax stands at \$31.0 billion, representing 28% of the government's consolidated revenue.

The average forecast differences for revenue from personal income tax were 0.2 percentage point in 2014-2015, 0.6 percentage point in 2015-2016 and 2.8 percentage points in 2016-2017.

— On average, the difference since 2014-2015 has been 1.2 percentage point.

For 2016-2017, the most significant forecast difference is due to downward adjustments of the growth of wages and salaries for 2016, which was forecast at 3.5% in the 2014-2015 budget and was ultimately stood at 2.6%.

TABLE 6

Forecast and observed change in personal income tax revenue (as a percentage and in percentage points)

	2014-2015	2015-2016	2016-2017
Budget 2014-2015	5.3	3.6	4.8
March 2015 Québec Economic Plan		4.7	4.7
March 2016 Québec Economic Plan			4.1
Observed⁽¹⁾	5.1	4.4	1.7
Mean deviation⁽²⁾	0.2	0.6	2.8

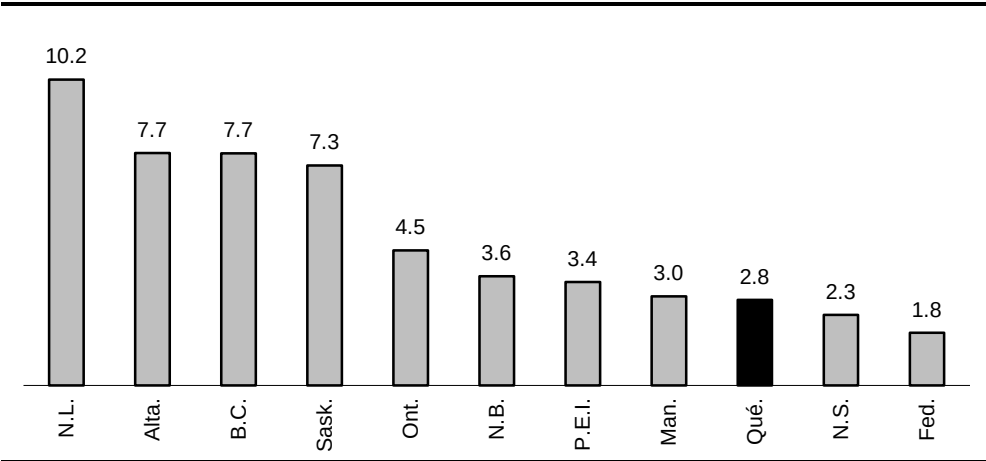
(1) According to the public accounts in the reference year.

(2) Average difference, in absolute value, between the changes observed and forecast in the various budgets for the given year.

Québec ranks third in Canada in terms of the accuracy of its forecast personal income tax revenue for the 2002-2003 to 2016-2017 horizon.

CHART 1

Mean deviation⁽¹⁾ in absolute values of personal income tax forecasts of Canadian provinces and the federal government from 2002-2003 to 2016-2017
(per cent)



(1) Represents the mean difference, as a percentage, between that observed in the public accounts for a given year and the forecasts produced in the corresponding budget.

Sources: Public accounts and budgets of the provinces and federal government for 2002-2003 to 2016-2017.
Calculations of the Ministère des Finances du Québec.

■ Corporate taxes

In 2018-2019, revenue from corporate income tax stands at \$8.3 billion, which represents nearly 8% of the government's consolidated revenue.

Corporate income tax is very volatile during an economic cycle, making it one of the most difficult sources of revenue to forecast. This volatility is partially due to the economic situation, as well as the particulars of the corporate tax system, which enable companies to manage their profits and losses according to the economic cycle.

- For example, during economic downturns, companies may have to make certain choices with regard to their income tax payable. They may choose to reduce their tax instalments or carry back losses incurred to a previous year in order to obtain a refund for part of the income tax paid during those years.
- Depending on the year, the fiscal choices made by companies can significantly intensify the effects related to the economy.

Due to the complexity of forecasting the behaviour of companies (availability of data, processing times for returns, and so on) and the impact of volatility on corporate income tax, larger forecast differences are expected.

The average forecast differences for corporate income tax revenue were 1.2 percentage point in 2014-2015, 11.4 percentage points in 2015-2016 and 2.6 percentage points in 2016-2017.

- Since 2014-2015, the mean deviation between corporate income tax forecasts and observed results has been 5.0 percentage points.

The bigger difference observed in 2015-2016 is mainly due to more sustained growth of tax revenues, primarily from tax installments.

- Furthermore, the tax measures implemented, particularly the elimination of the reduced rate for tax on capital for insurance companies applicable to individual insurance premiums and the temporary surtax for financial institutions, have spurred growth.

TABLE 7

Forecast and observed change in corporate income tax revenue
(as a percentage and in percentage points)

	2014-2015	2015-2016	2016-2017
Budget 2014-2015	5.0	5.0	4.5
March 2015 Québec Economic Plan		12.7	5.1
March 2016 Québec Economic Plan			2.5
Observed⁽¹⁾	3.8	20.2	6.6
Mean deviation⁽²⁾	1.2	11.4	2.6

(1) According to the public accounts in the reference year.

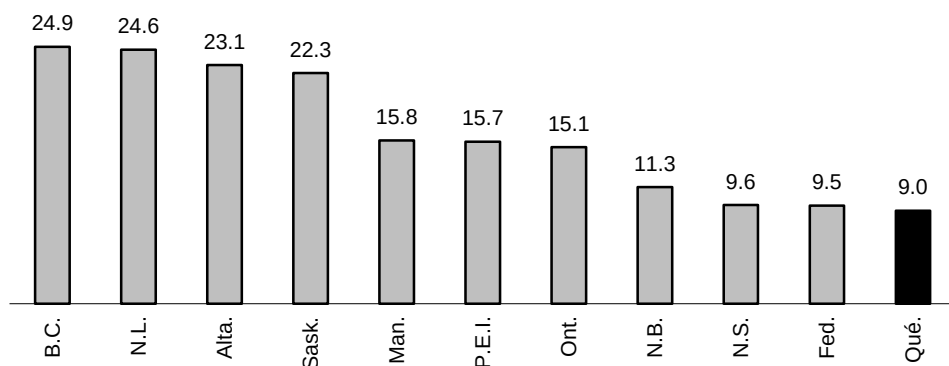
(2) Average difference, in absolute value, between the changes observed and forecast in the various budgets for the given year.

Despite the volatility of corporate income tax revenue, Québec is the Canadian jurisdiction that most accurately forecasts this type of revenue.

- With an average percentage difference of 9.0% since 2002-2003, Québec ranks first, above the federal government and Nova Scotia.

CHART 2

Mean deviation⁽¹⁾ in absolute values of corporate income tax forecasts of Canadian provinces and the federal government from 2002-2003 to 2016-2017
(per cent)



(1) Represents the mean difference, as a percentage, between that observed directly in the public accounts for a given year and the forecasts produced in the corresponding budget.

Sources: Public accounts and budgets of the provinces and federal government for 2002-2003 to 2016-2017.
Calculations of the Ministère des Finances du Québec.

■ Québec sales tax

Québec's sales tax revenue for 2018-2019 stands at \$17.1 billion, making it the second largest source of revenue. It represents more than 15% of the government's consolidated revenue.

Analysis of the differences in Québec sales tax forecasts shows differences of 1.5 percentage point in 2014-2015, 1.1 percentage point in 2015-2016 and 2.0 percentage points in 2016-2017.

TABLE 8

Forecast and observed change in sales tax revenue (as a percentage and in percentage points)

	2014-2015	2015-2016	2016-2017
Budget 2014-2015	3.6	4.1	2.8
March 2015 Québec Economic Plan		4.1	3.1
March 2016 Québec Economic Plan			3.9
Observed⁽¹⁾	2.1	5.2	5.3
Mean deviation⁽²⁾	1.5	1.1	2.0

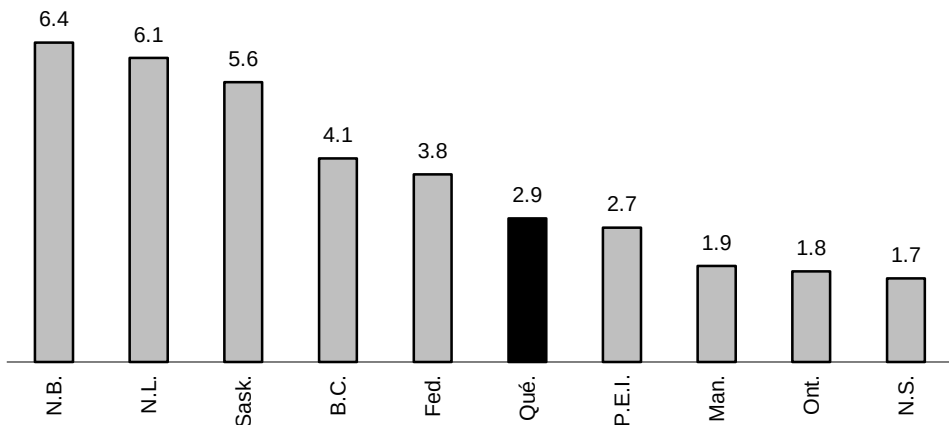
(1) According to the public accounts in the reference year.

(2) Average difference, in absolute value, between the changes observed and forecast in the various budgets for the given year.

The accuracy of the sales tax revenue forecast compares advantageously to that of the other provinces and the federal government.

CHART 3

Mean deviation⁽¹⁾ in absolute values of sales tax forecasts of Canadian provinces⁽²⁾ and the federal government from 2002-2003 to 2016-2017 (per cent)



(1) Represents the mean difference, as a percentage, between that observed directly in the public accounts for a given year and the forecasts produced in the corresponding budget.

(2) Alberta does not collect provincial sales tax.

Sources: Public accounts and budgets of the provinces and federal government for 2002-2003 to 2016-2017. Calculations of the Ministère des Finances du Québec.

❑ Mission expenditures forecast performance

The retroactive analysis of the differences in mission expenditures forecasts shows a mean deviation of 0.5 percentage point in 2014-2015, 0.3 percentage point in 2015-2016 and 0.9 percentage point in 2016-2017.

The difference is less than 1 percentage point for the three years.

TABLE 9

Forecast and observed change in mission expenditures
(as a percentage and in percentage points)

	2014-2015	2015-2016	2016-2017
Budget 2014-2015	1.9	1.3	1.7
March 2015 Québec Economic Plan		1.5	1.9
March 2016 Québec Economic Plan			2.4
Observed⁽¹⁾	1.4	1.1	2.9
Mean deviation⁽²⁾	0.5	0.3	0.9

(1) According to the public accounts in the reference year.

(2) Mean deviation, in absolute value, between the changes observed and forecast in the various budgets for the given year.

■ Québec ranks first when it comes to precision in expenditure forecasts

As is the case with own-source revenue forecasts, the expenditure forecasts of the Québec government are the most precise in Canada.

According to the C.D. Howe Institute, Québec ranks first when the standard deviation between the Québec government's expenditure forecasts over the past 15 years is compared to the standard deviation calculated by the provincial and federal governments.²¹

TABLE 10

Difference in forecasts for expenditure of provincial, territorial and federal governments from 2002-2003 to 2016-2017

	Difference ⁽¹⁾ (%)	Rank
Québec	1.1	1
Nova Scotia	2.0	2
Ontario	2.2	3
British Columbia	2.5	4
Prince Edward Island	2.5	5
New Brunswick	2.5	6
Manitoba	3.0	7
Federal government	3.5	8
Northwest Territories	3.9	9
Newfoundland and Labrador	4.6	10
Alberta	5.5	11
Saskatchewan	6.2	12
Nunavut	7.0	13
Yukon	7.1	14

(1) The root-mean-square error is used to measure the deviation.

Sources: Ministère des Finances for Québec and the C.D. Howe Institute for the other governments.

²¹ WILLIAM B. P. ROBSON, FARAH OMRAN, *Blown Budgets: Canada's Senior Governments Need Better Fiscal Controls*, Commentary No. 512, Toronto, C.D. Howe Institute, 2018, p. 8.

❑ Budgetary balance forecast performance

The budgetary balance is established based on revenue and expenditure forecasts and also by taking into account the principles outlined in the *Balanced Budget Act*. This act provides for the government's obligation to present balanced budgetary forecasts.

■ Accurate forecast

The budgetary balance is accurate. The mean deviation between the forecast balance and the observed balance is less than 1% of GDP.

In Québec's case, the accuracy of the observed budgetary balance is of particular importance when it comes to the *Balanced Budget Act*.

In relation to GDP, the mean deviation for the budgetary balance was 0.3% in 2014-2015, 0.5% in 2015-2016 and 0.6% in 2016-2017.

The biggest difference was observed in 2016-2017.

TABLE 11

Forecast and observed⁽¹⁾ change in the budgetary balance (millions of dollars)

	2014-2015	2015-2016	2016-2017
Budget 2014-2015	-1 049	1 583	2 254
March 2015 Québec Economic Plan		1 586	2 236
March 2016 Québec Economic Plan			2 028
Observed	136	3 644	4 362
Mean deviation⁽²⁾	1 185	2 060	2 189
% of GDP	0.3	0.5	0.6

(1) According to the public accounts in the reference year.

(2) Average difference between the levels observed and forecast in the various budgets for the given year.

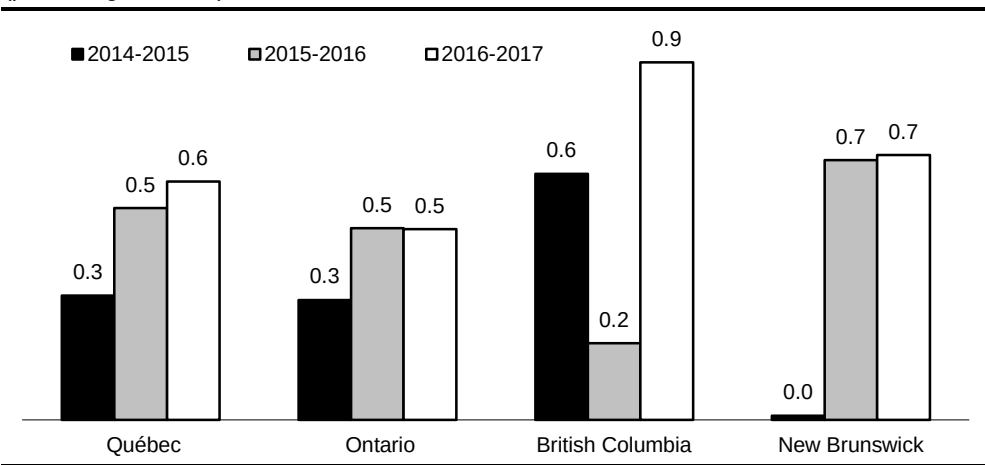
■ **Accuracy of budgetary balance forecast comparable to other provinces**

The analysis of the differences as a percentage of GDP between the budgetary balance forecast and observed from 2014-2015 to 2016-2017 for certain provinces shows that the accuracy in forecasting in Québec and the other provinces is comparable.

The actual budgetary balance has generally been higher than the forecast budgetary balance and the difference has been less than 1% of GDP for the analyzed period.

CHART 4

Difference between the forecast and observed budgetary balance of certain Canadian provinces
(percentage of GDP)



Sources: Budgets and public accounts of the provinces from 2014-2015 to 2016-2017.

3. PRUDENT BUDGETARY PROCESS

In addition to being transparent and rigorous, the budgetary process must meet a third expectation on the part of Quebecers: it must be prudent.

There are two reasons why prudence must be exercised.

- Forecasts are uncertain by nature and it is important that uncertainty be taken into account when defining the financial framework.
- A financial framework that is defined with all of the requisite rigour may be subject to internal and external shocks that are hard to foresee. Economic conditions could deteriorate rapidly and impact own-source revenue and certain expenditure categories.

☐ Taking uncertainties and risks into account

The budgetary process must take these uncertainties and risks into account.

- Forecasts of the various elements of the financial framework must be **drawn up with prudence**.
- The process also requires **coming up with a certain number of prudence margins** that may be used as required.

3.1 A prudent approach to drawing up forecasts

The process selected by the Québec government to draw up various forecasts that allow for the definition of the financial framework has just been presented. This process respects best practices so as to limit uncertainties and take risks into account.

- In order to reduce uncertainties and take certain risks into account, economic forecasts are systematically compared to the forecasts drawn up by private sector economists. The assumptions are cross validated, which allows for evaluation of the risks associated with the chosen scenarios.
- When it comes to own-source revenue, the Ministère des Finances reduces the risks associated with the forecast by carrying out detailed analyses for every revenue source and their respective components. The information required for drawing up forecasts is gathered and analyzed throughout the year, allowing for detailed tracking of the revenue collected and the changes in revenue.
- When it comes to mission expenditures forecasts and estimating the debt service, risks are also reduced by continuously analyzing the information used to draw up forecasts. Periodic tracking is carried out among government departments.

3.2 Margins for prudence to counter risks and uncertainty

Despite the prudent nature of the forecasts, it is essential to guard against risks and internal and external shocks by building up a certain number of margins that may be used as required.

□ Sensitivity analyses to determine the impact of risks

The sensitivity analyses drawn up by the Ministère des Finances and presented in the pre-election report²² show the potential impact, over the course of a year, of variations in certain assumptions for several elements of the financial framework. For example:

- a 1-percentage-point change in nominal GDP growth changes own-source revenue by roughly \$700 million;
- a variation of 1.0US¢/kWh in energy prices in external markets has an almost \$150 million impact on Hydro-Québec's net earnings in 2018;
- an increase of 1 percentage point in interest rates would increase the debt service by \$250 million.

²² For more information, see Section B of the pre-election report.

❑ Margins for prudence

In order to manage risk linked to uncertainties such as internal and external shocks, the government provides for margins in the form of financial provisions.

■ The reserves included in the financial framework

Three provisions are included in the financial framework.

- The contingency reserve is an overall reserve aimed at overcoming uncertainties that could influence the entire financial framework. This reserve allows the government to tackle various risks that result from changes in economic conditions.
- The Contingency Fund reserve is intended to cover unforeseen expenditures that may arise in government programs.
- The purpose of the debt service reserve is essentially to cover sudden fluctuations in financial markets. For example, the government could use the debt service reserve to cover a higher-than-anticipated increase in interest rates.

■ Stabilization reserve

Aside from the financial framework, the stabilization reserve is made up of the budgetary surpluses freed up and can be used to balance the financial framework.

The stabilization reserve is managed in compliance with the provisions of the *Balanced Budget Act*. It is a multi-year budgetary planning tool that is available to the government.

■ An overall margin of nearly \$11.2 billion over five years

Overall, the three provisions and the stabilization reserve as defined in the pre-election report should allow the government to counter risks that could affect the financial framework and result in either a decline in revenue or an increase in unexpected expenditure of \$11.2 billion.²³

²³ For more information on the sums forecast in the various margins for prudence, see page 44 of the highlights of the pre-election report.

4. FLEXIBLE BUDGETARY PROCESS

A transparent, rigorous and prudent budgetary process must also be flexible.

- Flexibility in the budgetary process is crucial in order to allow the government to quickly adapt to the economic and financial reality, based on formulated forecasts.
- Flexibility in the budgetary process is essential in order to give the government the means to adapt its policy direction implementation to reality and also allow the governments to revise its fiscal policy directions, that is, add new directions or abandon others.

☐ **Three instances where flexibility in the budgetary process is required**

The budgetary process implemented by the Québec government respects these flexibility requirements:

- when **updating information that defines the budgetary context**, due to factors that are often out of the government's control;
- when **gradually implementing government commitments**;
- when **making changes to budgetary choices**.

4.1 Updating data that define the budgetary context

Economic, financial and fiscal budgetary data are monitored on a practically permanent basis once the budget has been published. This process of monitored and subsequently updating budgetary data can lead the government to make certain changes to its actions.

These updates result in a revised financial framework approximately six months after the budget is published. The revised financial framework is published as part of the fall update.

Economic variables

The Ministère des Finances ensures that the various economic statistics and forecasts drawn up by private sector economists are monitored.

This monitored process is incorporated into a new forecasting exercise that begins each fall after the budget is tabled, as the fall update is being prepared. Forecasts are adjusted over the total period covered.

For example, when it comes to the March 2018 Québec Economic Plan, the economic forecasts for 2022, presented for the first time in 2018, will be revised twice a year until the 2023 fall update is published, allowing for almost 10 revisions.

❑ Revenue and expenditure

Forecasts for changes in revenue are also continuously monitored by the Ministère des Finances using reports produced throughout the year by Revenu Québec and the Comptroller of Finance, in particular.

The same applies to forecasts for changes in expenditure, which are monitored by the Secrétariat du Conseil du trésor, government departments, public bodies and government reporting entities.

■ Public accounts

The public accounts, tabled by the government, at the latest nine months following the end of the fiscal year, present the government's consolidated financial statements and information on revenue and expenditure. This information relates to revenue, expenditure of government departments and budget funded bodies as well as revenue, expenditure and investments of special funds and non-budget-funded bodies.

■ Fall update

The financial results published in the public accounts prompt the Ministère des Finances to revise the financial framework presented in the budget a few months beforehand. The financial framework that is corrected based on these results—and the changes made to economic forecasts—is made public as part of the fall update.

The publication of the fall update approximately six months after the budget clearly illustrates the flexibility inherent in the budgetary process and the fact that the data presented are not static.

4.2 Gradual implementation of government commitments

The government departments and responsible bodies gradually implement the government commitments announced in the Budget in the months or years following their announcement. This implementation may be completed faster than anticipated or, conversely, after additional time limits due to unforeseen difficulties.

The multi-year financing of government commitments allows for this gradual implementation process.

■ Government commitment implementation process

Information on the implementation of government commitments is gathered at the same time as information that defines the budgetary context.

The Ministère des Finances, in collaboration with all government departments and bodies, tracks the implementation of new initiatives that were announced in budgets.

— In addition, the government departments and bodies report on the use of any funds allocated to them.

Information on the implementation of government commitments that impacts any data for the previous fiscal year is integrated into the public accounts, which are tabled by the government, at the latest nine months following the end of the current fiscal year.

■ Fall update

As is the case with statistics that define the budgetary context, the fall update and subsequent budgets give the government an opportunity to make the necessary corrections to revenue and expenditure information, thus taking into account the reality of applying commitments announced by the government.

4.3 Changes to budgetary choices

The financial framework presented by the government when the budget is tabled may be revised at any time in order to take into account any changes to the budgetary context or the reality of implementing government commitments.

☐ Modifying previous choices

Flexibility in the budgetary process is required to allow the government to modify previous choices or implement new priorities.

When budgetary choices are modified or new priorities formulated, the process makes it possible to take into account new government decisions.

- The transparency of the process ensures that every Quebecer has the opportunity to be fully informed about the new choices that have been made, their impact on the budget and the consequences they will have on government policies.
- The stringent nature of the process means that the new choices will not jeopardize the quality of previous forecasts or forecast performance. It is essential that new budgetary choices be defined and financed while respecting the stringent nature of the financial framework, especially when it comes to the quality of economic, financial and fiscal forecasts.
- The same is true for the prudent approach to the process, which must not be compromised when new choices are made by the government.

❑ **The financial framework: a common base and an integral part of the democratic process**

The financial framework presented by the government when the budget is tabled is not a collection of static figures that cover a five-year period, but a consistent and comprehensive presentation of choices and commitments defined by the government and presented to Quebecers at a certain point in time.

This financial framework, which is presented in the form of the *Pre-election Report on the State of Québec's Public Finances – August 2018*, is both a reference and a common base for all Quebecers and political parties who can present their own budgetary plan by clearly explaining how the plan will be financed.

Therefore, the financial framework is an integral component of the democratic debate in that its process guarantees quality.

