Annual Financial Report

of the Government of Canada

Fiscal Year 2001–2002

Canada

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A budgetary surplus of $8.9 billion was recorded in 2001-02. This marks the fifth consecutive year in which the federal government has recorded a surplus – the last time this occurred was in the period up to 1951-52. As a result of the budgetary surpluses recorded since 1997-98, the net debt has been reduced by $46.7 billion to $536.5 billion from its peak of $583.2 billion in 1996-97.

The federal government achieved a surplus in an environment in which most other major economies recorded deficits. This is attributable to stronger-than-expected economic growth in the latter half of the fiscal year and prudence in budget planning, ensuring that monies are not committed without the assurance that we will not go back into deficit.

Because of this prudence, even in the uncertain economic environment of 2001, the Government was able to act to address a number of key priorities. It legislated and implemented the tax cuts announced in the February 2000 budget and October 2000 *Economic Statement and Budget Update*, which provided timely stimulus to the economy. In addition, in the aftermath of the September 11th terrorist attacks, it acted quickly to enhance the security of Canadians and to provide a boost to confidence in the economy.

Department of Finance Canada
Ministère des Finances Canada

Net debt as a percentage of the economy was just over 49 per cent in 2001-02, a reduction of almost 22 percentage points from its peak of about 71 per cent in 1995-96. On an international basis Canada has made more progress in reducing its debt burden than any other Group of Seven (G-7) country. According to the Organisation for Economic Co-operation and Development, Canada's net debt burden is now below the G-7 average – well below those in Italy and Japan and in line with those in Germany and France. Only the United Kingdom and the United States have lower debt levels.

This large reduction in public debt is important for a variety of reasons. A lower debt burden means that a smaller portion of the revenue the Government collects from taxpayers must go towards debt-servicing payments, thereby leaving more resources for reducing taxes and funding valued programs and services. A lower debt burden also lessens the exposure of Canada's fiscal situation to economic shocks, especially an increase in interest rates or prolonged slowdowns in economic activity. And a lower debt burden reduces the amount that younger Canadians will have to pay for servicing debt incurred by the generations that preceded them.

The financial data in this report are based on the audited results, which will appear in more detail in the 2002 *Public Accounts of Canada*, scheduled for tabling in the House of Commons this fall. They cover the federal government's spending and revenue performance for the past fiscal year (April 1, 2001 to March 31, 2002) and detail the factors affecting these results. In addition, the *Fiscal Reference Tables* publication has been updated to incorporate the results for 2001-02 and historical revisions to the *National Economic and Financial Accounts* published by Statistics Canada. These tables are an integral part of this report.

The Honourable John Manley, P.C., M.P.
Deputy Prime Minister and Minister of Finance

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Note to Readers

The Canada Customs and Revenue Agency (CCRA) collects personal income taxes on behalf of the Government and all provincial and territorial governments except Quebec. On January 29, 2002, the CCRA announced it had identified a problem in tax accounting that resulted in overpayments to provinces under the tax collection agreements. On September 4, 2002, the Minister of Finance announced that the Government of Canada would recover $1.4 billion of the amounts overpaid for the years 1997 to 1999 and use the money to pay down the debt. The net present value of these amounts has been recast to the fiscal years to which they apply. In addition, once the problem was discovered, the federal government took immediate action to prevent further overpayments related to 2000 and subsequent taxation years. This has resulted in a transfer of $1 billion from the tax collection agreements with respect to taxation year 2000 to budgetary revenues in 2000-01. As a result, the budgetary surplus has been revised upward beginning in 1997-98 as shown in the table below.

Revisions to the Budgetary Surplus

	Originally published	Revised
	($ billions)	
1997-98	3.5	3.8
1998-99	2.9	3.1
1999-00	12.3	12.7
2000-01	17.1	18.1

REPORT HIGHLIGHTS

- A budgetary surplus of $8.9 billion was achieved in 2001-02. This marks the fifth consecutive year the federal budget has been in surplus.
- Net debt has been reduced by $46.7 billion over the last five years. As a result, Canada's net debt at the end of 2001-02 was $536.5 billion.
- The net debt-to-GDP (gross domestic product) ratio is now 49.1 per cent, down sharply from its peak of 70.9 per cent in 1995-96. It is now at its lowest level since 1984-85.
- Market debt – the debt issued on credit markets – as a percentage of GDP has declined to 40.5 per cent from the peak of 57.9 per cent in 1995-96. Foreign holdings declined to 17 per cent of market debt – its lowest ratio since 1986-87.
- The revenue-to-GDP ratio fell to 15.9 per cent in 2001-02, down sharply from 16.9 per cent in 2000-01. This decline reflects, in part, the impact of the tax reductions announced in the February 2000 budget and October 2000 *Economic Statement and Budget Update*.
- Program spending increased 6.1 per cent in 2001-02, of which over 80 per cent was attributable to increased transfers to the provinces and territories under the historic agreements reached by first ministers in September 2000 and higher employment insurance benefits.
- Public debt charges as a percentage of revenues were 21.8 per cent in 2001-02, down from the peak of 36 per cent in 1995-96. This is the lowest the ratio has been since 1979-80.

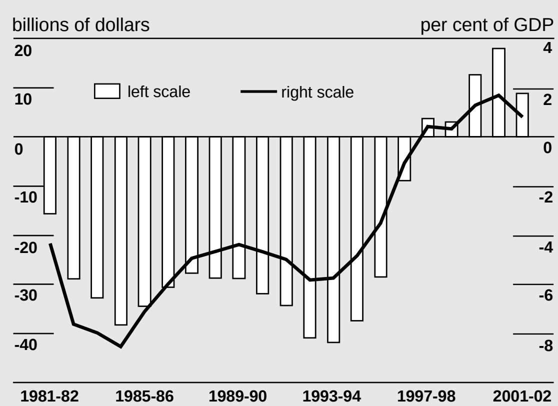
The Budgetary Balance

Economic growth in most major economies slowed sharply in the first half of 2001, reflecting the impact of higher interest rates and energy prices and a sharp decline in global high technology investment. The events of September 11th introduced a further shock to the global economy through disruptions in economic activity and sharp declines in confidence. Like all other countries, Canada was impacted by these developments. Economic growth slowed considerably, from 4.5 per cent in 2000 to only 1.5 per cent in 2001.

However, Canada was much better positioned to cope with the global slowdown than in previous global downturns due to much healthier finances, the timely tax reductions announced in the October 2000 *Economic Statement and Budget Update*, low and stable inflation, declining net foreign debt and historically low interest rates. As a result, the economy did not slow as much as in other countries. Indeed, Canada avoided the U.S. recession and growth rebounded strongly in the first half of 2002.

In the October 2000 *Economic Statement and Budget Update*, May 2001 *Economic Update* and December 2001 budget, the Government committed to a balanced budget or better for 2001-02. The final budgetary surplus for 2001-02 was $8.9 billion. All of this has been applied to reducing Canada's net debt.

Budgetary Balance



Sources: *Public Accounts of Canada* and Statistics Canada.

The budgetary balance went from a deficit of 5.8 per cent of GDP ($42 billion) in 1993-94 to five consecutive surpluses over the 1997-98 to 2001-02 period. The 2001-02 surplus was 0.8 per cent of GDP ($8.9 billion). Nearly three-quarters of the improvement from 1993-94 is attributable to the decline in program spending – from 16.5 per cent of GDP in 1993-94 to 11.6 per cent of GDP in 2001-02, with the remainder attributable to lower public debt charges.

Net Debt

The 2001-02 surplus of $8.9 billion brings the federal government's net debt – the accumulation of annual deficits and surpluses – down to $536.5 billion from its peak of $583.2 billion in 1996-97. As a share of GDP, net debt dropped to 49.1 per cent in 2001-02, down nearly 22 percentage points from the peak of 70.9 per cent in 1995-96. This ratio is generally recognized as the most appropriate indicator of the debt burden as it measures debt relative to the ability of the Government and the country's taxpayers to finance it. This is the sixth consecutive year in which the debt-to-GDP ratio has declined, and it is the lowest the ratio has been since 1984-85.

Net debt consists of interest-bearing debt and other liabilities, net of financial assets. Interest-bearing debt, in turn, consists of unmatured, or market, debt and the Government's obligations to internally held accounts – primarily the liabilities for the federal government employees' pension plans. In 2001-02 total interest-bearing debt declined by $5.8 billion: market debt declined by $4.1 billion and obligations to pension accounts declined by $1.7 billion. Other liabilities fell by $3.0 billion, while financial assets increased by $0.1 billion.

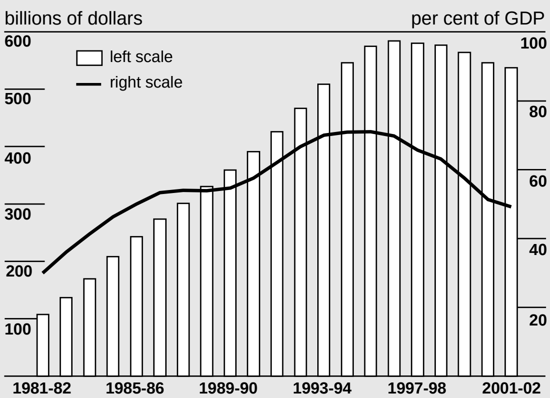
Financial Requirements/Source

Financial requirements/source measures the difference between cash coming in to the Government and cash going out. Most industrialized countries use a measure comparable to the financial requirements/source as their main measure of the budgetary balance.

There was a financial source (excluding foreign exchange transactions) of $4.7 billion in 2001-02 – the sixth consecutive year Canada has recorded a financial source – the only G-7 country to do so.

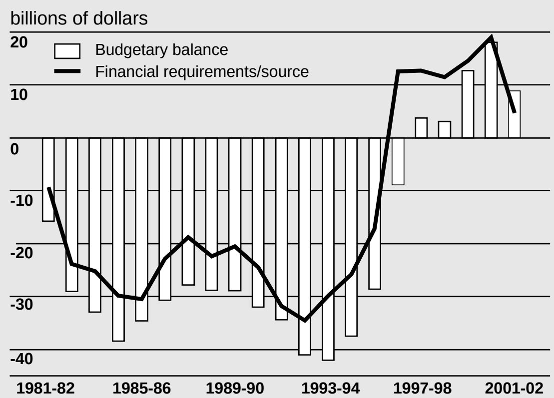
In 2001-02 there was a net requirement of $1.8 billion relating to foreign exchange transactions, down from a net requirement of $8.8 billion in 2000-01. Including this amount, the financial source in total was $2.9 billion, down from a source of $10.2 billion in 2000-01.

Net Debt



Sources: *Public Accounts of Canada* and Statistics Canada.

Budgetary Balance and Financial Requirements/Source



Note: Excludes foreign exchange transactions.
Source: *Public Accounts of Canada*.

Table 1
Financial Highlights

	1997-98	1998-99	1999-00	2000-01	2001-02
			($ billions)		
Budgetary transactions					
Revenues	153.5	155.9	166.1	179.6	173.3
Program spending	-108.8	-111.4	-111.8	-119.3	-126.7
Operating balance	44.8	44.5	54.4	60.2	46.6
Public debt charges	-40.9	-41.4	-41.6	-42.1	-37.7
Budgetary balance	**3.8**	**3.1**	**12.7**	**18.1**	**8.9**
Non-budgetary transactions	8.9	8.4	1.9	0.8	-4.2
Financial requirements/source (excluding foreign exchange transactions)	12.7	11.5	14.6	19.0	4.7
Foreign exchange transactions	-2.2	-5.7	-6.8	-8.8	-1.8
Net financial requirements/source	10.6	5.8	7.7	10.2	2.9
Net change in borrowings	-9.6	-6.9	-4.0	-10.0	-4.1
Net change in cash balances	1.0	-1.1	3.7	0.2	-1.2
Financial position					
Total liabilities	-638.5	-640.3	-638.7	-632.9	-624.1
Total financial assets	59.2	64.0	75.1	87.5	87.6
Accumulated deficit (net debt)	-579.4	-576.3	-563.5	-545.4	-536.5
Financial results (% of GDP)					
Budgetary revenues	17.4	17.0	16.9	16.9	15.9
Program spending	12.3	12.2	11.4	11.2	11.6
Public debt charges	4.6	4.5	4.2	4.0	3.5
Budgetary balance	0.4	0.3	1.3	1.7	0.8
Net debt	65.6	63.0	57.5	51.2	49.1

Note: Results for 1997-98 to 2000-01 have been revised to reflect the misclassification of mutual fund trust capital gain refunds.

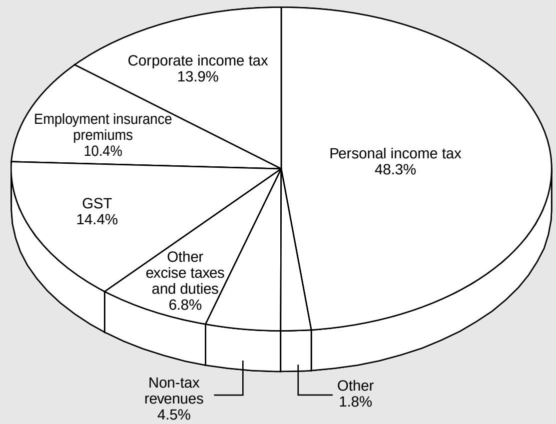
BUDGETARY REVENUES

Reflecting much slower growth in 2001 and the tax reductions introduced in the October 2000 *Economic Statement and Budget Update*, budgetary revenues declined by $6.3 billion, or 3.5 per cent, to $173.3 billion in 2001-02 after advancing by 8.1 per cent in the previous year. Declines were spread throughout most major components, with the exception of personal income tax revenues and excise taxes and duties (see Table 2). Even in these latter two components, the rates of increase were substantially less than those recorded in the previous fiscal year. This primarily reflected the impact of the global economic weakness on the various tax bases and the effect of the tax reduction measures announced in the February 2000 budget and October 2000 *Economic Statement and Budget Update*. These measures included the reduction in personal income tax rates; the elimination of the 5-per-cent surtax; increases in thresholds; the restoration of full indexation of the personal income tax system; and increases in the Canada Child Tax Benefit.

Personal income tax revenues, the largest component of budgetary revenues, were up only $0.5 billion, or 0.6 per cent, in 2001-02 due entirely to prior-year adjustments and the timing of receipts.

- Gross remittances received include federal personal income tax, provincial income tax collected by the Canada Customs and Revenue Agency (CCRA) under the tax collection agreements with participating provinces, as well as employer and employee premiums for employment insurance (EI) and the Canada Pension Plan (CPP). Estimates are made for these various components on a monthly basis, with adjustments made once either preliminary or final data become available from the CCRA. In 2001-02 there were transfers of about $500 million from the EI and CPP accounts to personal income tax relating to overestimations of deductions for previous fiscal years.

Composition of Net Revenues for 2001-02



Note: Numbers do not add to 100% due to rounding.
Source: *Public Accounts of Canada*.

- There are also important collection lags between the economic event giving rise to personal income tax liabilities and the receipt of revenues. In April and May 2001 extraordinarily large final tax payments were received with respect to the 2000 taxation year, in large part due to the strong increases in capital gains realizations in 2000. Excluding the impact of the above factors, personal income tax revenues would have recorded a significant decline, reflecting the impact of tax reductions and weakness in economic growth.

Corporate income tax revenues declined $4.2 billion in 2001-02, or 14.9 per cent, following an increase of 21.8 per cent in 2000-01. This decline primarily reflected an estimated 8.9-per-cent decline in corporate profits. In addition, the December 2001 budget announced a six-month deferral of small business corporate income tax instalments for the last quarter of 2001-02 to assist small businesses with the economic slowdown. It is estimated that this measure reduced corporate income tax revenues in 2001-02 by about $600 million.

Table 2

Net Budgetary Revenues

	2000-01	2001-02	Net Change	
		($ millions)		(%)
Net income tax collections				
Personal income tax	83,305	83,790	485	0.6
Corporate income tax	28,212	24,013	-4,199	-14.9
Other	4,312	3,035	-1,277	-29.6
Total	115,829	110,838	-4,991	-4.3
Employment insurance premium revenues	18,731	17,980	-751	-4.0
Net excise taxes and duties				
Goods and services tax	24,990	24,909	-81	-0.3
Customs import duties	2,807	3,018	211	7.5
Other excise taxes/duties				
Energy taxes	4,805	4,758	-47	-1.0
Other	3,514	3,953	439	12.5
Total	8,319	8,711	392	4.7
Total	36,116	36,638	522	1.4
Net tax revenues	170,676	165,456	-5,220	-3.1
Net non-tax revenues				
Return on investments	6,144	5,892	-252	-4.1
Other non-tax revenues[1]	2,770	1,967	-803	-29.0
Total	8,914	7,859	1,055	-11.8
Net budgetary revenues	**179,590**	**173,315**	**-6,275**	**-3.5**

Note: Personal income tax revenues for 2000-01 have been revised to reflect the misclassification of mutual fund trust capital gain refunds.

[1] "Refunds from previous years' expenditures" was reclassified from "Other non-tax revenues" to program spending. This has the effect of reducing revenues and program spending by $578 million.

Other income tax revenues were down $1.3 billion, or 29.6 per cent, primarily due to a consolidation adjustment relating to refundable taxes withheld from the federal Retirement Compensation Arrangements Account that were previously credited to tax revenues.

EI premium revenues were down $0.8 billion, or 4.0 per cent, as prior-year adjustments and the decline in premium rates more than offset the impact of the growth in the number of people employed and therefore paying premiums. The employee premium rate (per $100 of insurable earnings) was reduced from $2.40 for 2000 to $2.25 for 2001 and $2.20 for 2002 (with a corresponding decline in the employer rate).

Excise taxes and duties increased $0.5 billion, or 1.4 per cent. However, there were significant variations among the various components.

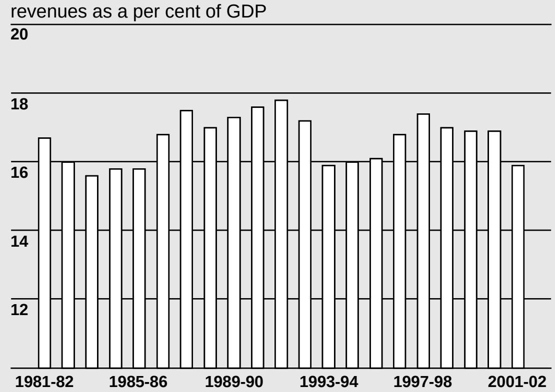
- Goods and services tax (GST) revenues were marginally lower, reflecting declines in GST collected on imported goods and higher rebates.
- Customs import duties increased $0.2 billion, or 7.5 per cent.
- Other excise taxes and duties were up 4.7 per cent, primarily due to the increase in excise tax rates on tobacco products. Energy taxes were slightly lower, reflecting lower taxes collected on aviation fuel.

Non-tax revenues declined $1.1 billion, or 11.8 per cent, in 2001-02, primarily reflecting lower Bank of Canada profits and interest on bank balances due to the decline in interest rates. In addition, "refunds from previous years' expenditures," which in previous years was included as part of "other non-tax revenues," is now netted against program spending. This has the effect of lowering both budgetary revenues and program spending by an equivalent amount, with no impact on the overall budgetary balance.

The revenue ratio – budgetary revenues as a percentage of GDP – represents a comprehensive measure of the overall "tax burden" in that it compares the total of all revenues collected to the size of the economy. The revenue ratio stood at 15.9 per cent in 2001-02, compared to 16.9 per cent in 2000-01. It is now at its lowest level since 1993-94. The decline in the ratio between 2000-01 and 2001-02 reflects the impact of the tax reductions announced in the February 2000 budget and the October 2000 *Economic Statement and Budget Update*, as well as the impact of the global economic slowdown.

It should be noted that some important components of income subject to taxation are excluded from the Statistics Canada measure of GDP, such as capital gains and income from trusteed pension plans. As a result, this ratio overstates the tax burden. In addition, the sharp rise in capital gains and the growth in income from trusteed pension plans due to the aging of the population distort year-to-year changes in the ratio. Therefore, caution should be exercised in interpreting this ratio.

Revenue Ratio



Sources: Department of Finance and Statistics Canada.

The figures in Table 2 are presented on a "net" basis, reflecting the way in which revenues and expenditures are presented to Parliament and in the Government's annual budget. In this presentation, the Canada Child Tax Benefit, the quarterly GST credit and the repayments of Old Age Security benefits are netted against income tax revenues. Certain departmental revenues, such as the revenues of consolidated Crown corporations and revenues levied by departments for specific services (such as the contract costs of policing services in provinces), are netted against spending. This classification has the effect of reducing both revenues and spending but has no impact on the budgetary balance.

Table 3 shows the impact of "grossing up" budgetary revenues for these adjustments. In 2001-02 they amounted to $14.2 billion, of which over half was due to the Canada Child Tax Benefit. As a result, gross budgetary revenues were $187.5 billion in 2001-02, down 3 per cent from 2000-01.

Table 3
Gross Budgetary Revenues

	2000-01	2001-02	Net Change	
		($ millions)		(%)
Net budgetary revenues	**179,590**	**173,315**	**-6,275**	**-3.5**
Adjustments				
Canada Child Tax Benefit	6,811	7,557	746	11.0
Old Age Security benefit repayments	-588	-734	-146	24.8
Quarterly GST credit	2,901	2,964	63	2.2
Revenues netted against expenditures	2,874	2,936	62	2.2
Revenues of consolidated Crown corporations	1,762	1,429	-333	-18.9
Net adjustment	13,760	14,152	392	2.8
Gross budgetary revenues	**193,350**	**187,467**	**-5,883**	**-3.0**

BUDGETARY EXPENDITURES

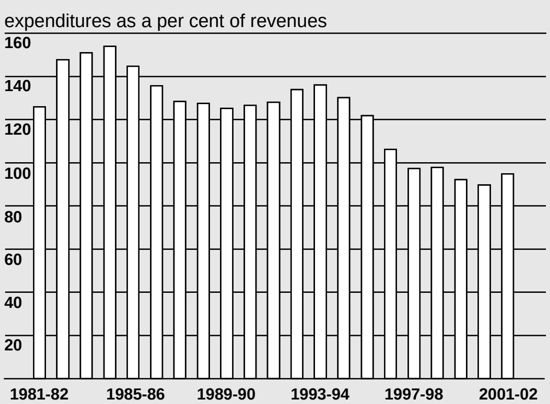
Budgetary expenditures consist of two major components – public debt charges and program spending. Net budgetary expenditures amounted to $164.4 billion in 2001-02, up $3.0 billion, or 1.8 per cent, from 2000-01 (see Table 4). Public debt charges declined $4.4 billion, or 10.4 per cent, while program spending advanced $7.3 billion, or 6.1 per cent. Program spending in 2001-02 was $126.7 billion.

The expenditure ratio – budgetary expenditures as a percentage of net budgetary revenues – stood at 94.9 per cent in 2001-02, up from 89.9 per cent in 2000-01. This increase reflects the impact of both the decline in budgetary revenues and the increase in budgetary expenditures. In 1993-94 the expenditure ratio stood at 136.2 per cent.

Public debt charges declined by $4.4 billion, or 10.4 per cent, to $37.7 billion in 2001-02, primarily attributable to a decline in the stock of interest-bearing debt and lower average effective interest rates on that debt. For the first time since 1985-86 public debt charges are no longer the largest component of budgetary expenditures. At 23.0 per cent of total expenditures, they are slightly less than transfers to persons (elderly and EI benefits).

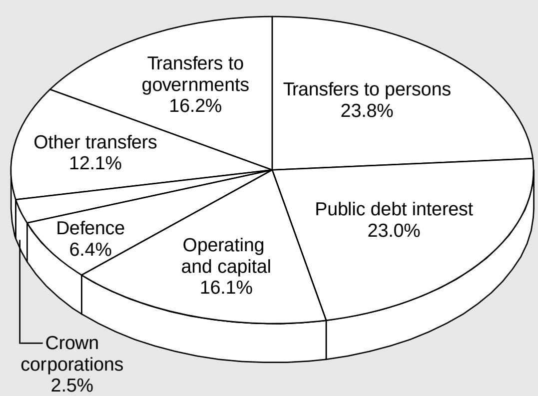
- The average effective interest rate on the Government's interest-bearing debt (unmatured debt and pension liabilities) was 6.9 per cent in 2001-02, compared to 7.6 per cent in 2000-01. The average effective interest rate on unmatured debt was 6.2 per cent while that on pension and other accounts was 9.1 per cent.
- The stock of total interest-bearing debt declined by $5.8 billion in 2001-02, from $589.2 billion to $583.4 billion, as the stock of market debt declined by $4.1 billion to $442.3 billion, while liabilities to pension and other accounts fell by $1.7 billion to $141.2 billion. This is the first year in which liabilities to pension and other accounts have declined, attributable to the impact of the reform of federal employees' pension plans, whereby current contributions are invested in the markets by the Public Sector Pension Investment Board and assets related to a number of Crown corporations are being transferred to them as they establish their plans.

Expenditure Ratio



Source: Department of Finance.

Composition of Net Expenditures for 2001-02



Note: Numbers do not add to 100% due to rounding.
Source: *Public Accounts of Canada*.

Table 4
Net Budgetary Expenditures

	2000-01	2001-02	Net Change	
		($ millions)		(%)
Net major transfers to persons				
Elderly benefits	24,256	25,365	1,109	4.6
Employment insurance benefits	11,444	13,748	2,304	20.1
Relief for Heating Expenses	1,459		-1,459	
Total	37,159	39,113	1,954	5.3
Major transfers to other levels of government				
Canada Health and Social Transfer	13,500	17,300	3,800	28.1
Medical Equipment Fund	1,000		-1,000	
Fiscal arrangements	12,684	11,978	-706	-5.6
Alternative Payments for Standing Programs	-2,460	-2,662	-202	8.2
Total	24,724	26,616	1,892	7.7
Net direct program spending				
Subsidies and other transfers				
Agriculture and Agri-Food	1,822	1,897	75	4.1
Foreign Affairs and International Trade	2,358	2,405	47	2.0
Health Canada	1,302	1,617	315	24.2
Human Resources Development	1,995	1,698	-297	-14.8
Indian Affairs and Northern Development	4,448	4,557	109	2.5
Industry/regional agencies	2,079	2,628	549	26.4
Veterans Affairs	1,463	1,557	94	6.4
Canada Foundation for Innovation	1,250		-1,250	
Canada Health Infoway Inc.	500		-500	
Other	3,827	3,495	-332	-8.7
Total	21,044	19,854	-1,190	-5.7
Crown corporations				
Canada Mortgage and Housing Corporation	1,906	1,910	4	0.2
Canadian Broadcasting Corporation	902	983	81	9.0
Other	95	1,189	1,094	1,151.6
Total	2,903	4,082	1,179	40.6
Operating and capital expenditures				
Defence	9,696	10,571	875	9.0
All other departments	23,822	26,437	2,615	11.0
Total	33,518	37,008	3,490	10.4
Net direct program spending	57,465	60,944	3,479	6.1
Net program spending[1]	**119,348**	**126,673**	**7,325**	**6.1**
Public debt charges	42,094	37,735	-4,359	-10.4
Net budgetary expenditures	**161,442**	**164,408**	**2,966**	**1.8**

[1] "Refunds from previous years' expenditures" was reclassified from "Other non-tax revenues" to program spending. This has the effect of reducing revenues and program spending by $578 million.

The interest ratio – public debt charges as a percentage of net budgetary revenues – declined from 23.4 per cent in 2000-01 to 21.8 per cent in 2001-02. This ratio means that, in 2001-02, the Government spent less than 22 cents of every revenue dollar on interest on the public debt. This is down from the peak of 36 cents in 1995-96 and is the lowest this ratio has been since the late 1970s. This is money that must be paid to meet the Government's obligations on its debt. The lower the ratio, the more flexibility the Government has to address the key priorities of Canadians.

Program spending amounted to $126.7 billion in 2001-02, an increase of $7.3 billion, or 6.1 per cent, from 2000-01. Higher cash transfers to provinces and territories under the Canada Health and Social Transfer (CHST) and increased EI benefits accounted for over 80 per cent of the increase in program spending. All major components were higher, with the exception of subsidies and other transfers.

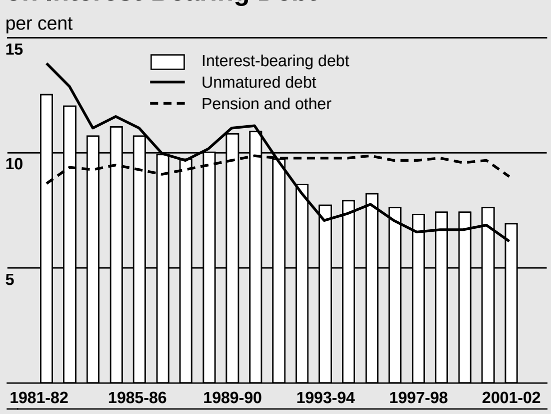
Major transfer payments to persons increased by $2.0 billion, or 5.3 per cent.

- Elderly benefits consist of Old Age Security, Guaranteed Income Supplement and spouse's allowance payments. Total benefits were up $1.1 billion in 2001-02, reflecting both higher average benefits, which are indexed to inflation, and an increase in the number of recipients.
- EI benefits increased $2.3 billion in 2001-02. About half of this increase was attributable to increased regular benefit payments, reflecting the deterioration in the labour market and the accompanying increase in the number of unemployed. Most of the remaining increase was due to higher special benefits, in particular the increase in parental benefits, reflecting the doubling of parental leave from six months to one year.
- Partially offsetting the impact of these developments was the one-time Relief for Heating Expenses for low- and modest-income Canadians of $1.5 billion that was paid in January 2001.

Major transfer payments to other levels of government include the CHST, fiscal arrangements (equalization, transfers to the territories, as well as a number of small transfer programs) and Alternative Payments for Standing Programs. Net cash transfers increased by $1.9 billion in 2001-02, or 7.7 per cent.

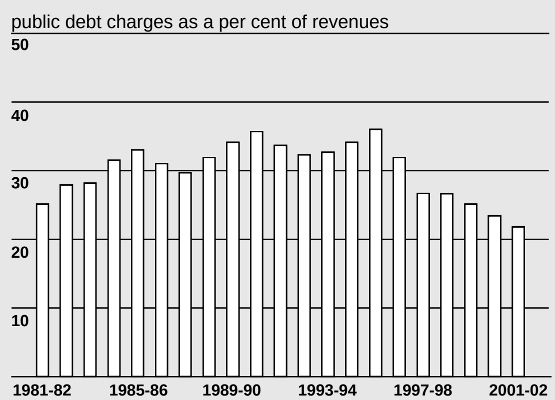
- The CHST – a block-funded transfer – supports health care, post-secondary education, social assistance and social services, including early childhood development. It provides support in the form of cash and tax transfers to the provinces and territories. As part of the September 2000 Agreements

Average Effective Interest Rate on Interest-Bearing Debt



Sources: *Public Accounts of Canada* and Department of Finance.

Interest Ratio



Source: Department of Finance.

on Health Renewal and Early Childhood Development, the federal government legislated $21.1 billion of additional cash to be provided under the CHST over the next five years. As part of this, an incremental $3.8 billion was paid in 2001-02.

- Total entitlements under fiscal arrangements decreased by $0.7 billion, or 5.6 per cent, primarily due to prior-year adjustments affecting equalization entitlements. Under the equalization program, the federal government transfers funds to the less prosperous provinces so that they can provide their residents with public services comparable to those in other provinces without having to resort to higher-than-average taxation. Equalization legislation is renewed every five years. The current legislation, which covers the period 1999-2000 to 2003-04, capped total entitlements in 1999-2000 at $10 billion, with the annual maximum entitlements growing in line with the growth in nominal GDP. The weak growth in nominal GDP in 2001 restrained the overall increase in equalization entitlements for 2001-02. In addition, in September 2000 the federal government indicated that the cap for 1999-2000 only would be lifted, resulting in an incremental entitlement for that year of about $0.8 billion. Under the Government's accounting rules, this amount was charged to 2000-01, thereby accounting for most of the decline between 2000-01 and 2001-02. Finally, transfers to the territories were lower due to recoveries resulting from overpayments in previous years.

- The Alternative Payments for Standing Programs represent recoveries of federal tax point abatements under contracting-out arrangements. These arrangements allow provinces to assume the administrative and financial authority for certain federal-provincial programs. In turn, the federal government provides provinces with tax points, the value of which are netted against total entitlements and accordingly recovered from cash transfers. These recoveries reflect the growth in the value of the tax points.

- Also affecting the year-over-year change was a one-time payment in 2000-01 of $1 billion to a third-party trust for provinces and territories to acquire new medical equipment. This was part of the September 2000 Agreements on Health Renewal and Early Childhood Development.

Direct program spending – total program spending less major transfers to persons and other levels of government – consists of subsidies and other transfer payments, expenditures related to Crown corporations, and operating and capital expenditures of departments and agencies, including National Defence. This spending amounted to $60.9 billion in 2001-02, up $3.5 billion, or 6.1 per cent, from 2000-01. Within direct program spending:

- Subsidies and other transfer payments decreased by $1.2 billion, or 5.7 per cent, primarily reflecting the impact of one-time transfers made in 2000-01. These included:
  - $1.25 billion to the Canada Foundation for Innovation (CFI) to award funds to help post-secondary educational institutions, research hospitals and not-for-profit institutions modernize their research infrastructure and assist in associated operating and maintenance costs. The Government's total transfer to the CFI to date is $3.15 billion.
  - $500 million to the Canada Health Infoway Inc. to accelerate the development and adoption of modern systems of information technology to provide better health care. This investment was part of the September 2000 Agreements on Health Renewal and Early Childhood Development.

- Expenditures related to Crown corporations were up $1.2 billion to $4.1 billion in 2001-02. This component includes appropriations to consolidated Crown corporations (those Crown corporations that rely on government funding as their principal source of revenue) and the annual profit and losses of enterprise Crown corporations. Most of the annual increase was attributable to lower net profits of enterprise Crown corporations.

- Operating and capital expenditures include the costs of defence, government administration and delivery of specific services to the public, such as:

  – health care to Aboriginals and veterans;

  – research undertaken by government departments;

  – food inspection;

  – Coast Guard and air and sea rescue;

  – operation of national parks and historic sites;

  – collection of taxes;

  – operation of federal correctional institutions and provision of police services; and

  – administration of programs.

  This spending increased by $3.5 billion, or 10.4 per cent, in 2001-02. Of this amount:

  – Defence spending increased by $0.9 billion, or 9.0 per cent, primarily due to increased funding related to meeting Canada’s international commitments.

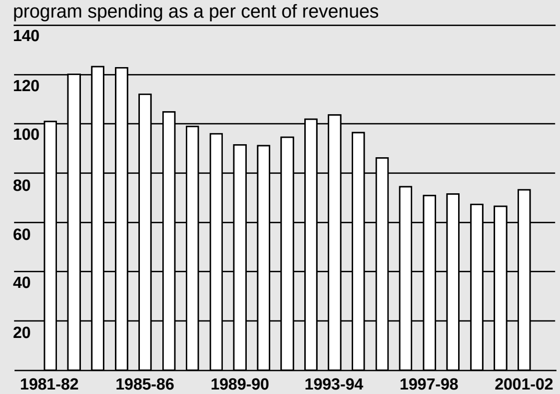
  – Non-defence departmental operating and capital spending increased by $2.6 billion. About half of this increase was attributable to new policy initiatives announced during the year, particularly those associated with the implementation of enhanced personal and economic security.

The program share – program spending as a percentage of budgetary revenues – amounted to 73.1 per cent, up from 66.5 per cent 2000-01. In 1993-94 the program share was 103.5 per cent.

The above numbers are presented on a “net” basis, as discussed in the previous section, “Budgetary Revenues.” Table 5 shows the impact of the adjustments. Gross expenditures are $14.2 billion higher than net expenditures.

Program Share

program spending as a per cent of revenues



Source: Department of Finance.

Table 5

Gross Budgetary Expenditures

	2000-01	2001-02	Net Change	
		($ millions)		(%)
Net budgetary expenditures	**161,442**	**164,408**	**2,966**	**1.8**
Adjustments				
Canada Child Tax Benefit	6,811	7,557	746	11.0
Old Age Security benefit repayments	-588	-734	-146	24.8
Quarterly GST credit	2,901	2,964	63	2.2
Revenues netted against expenditures	2,874	2,936	62	2.2
Revenues of consolidated Crown corporations	1,762	1,429	-333	-18.9
Net adjustment	13,760	14,152	392	2.8
Gross budgetary expenditures	**175,202**	**178,560**	**3,358**	**1.9**

THE BUDGETARY BALANCE, FINANCIAL REQUIREMENTS/SOURCE AND DEBT

The budgetary balance is the most comprehensive measure of the federal government's fiscal results. It is presented on a modified accrual basis of accounting, largely recording government liabilities when they are incurred, regardless of when the cash payment is made, and recording tax revenues only when cash is received. The budgetary balance covers only those activities over which the Government has legislative control.

In contrast, financial requirements/source measures the difference between cash coming in to the Government and cash going out. It differs from the budgetary balance in that it includes transactions in loans, investments and advances, federal employees' pension accounts, other specified purpose accounts, and changes in other financial assets and liabilities. These activities are included as part of non-budgetary transactions. The conversion from modified accrual to cash accounting is also reflected in non-budgetary transactions. Non-budgetary transactions in 2001-02 resulted in a net requirement of funds amounting to $4.2 billion, compared to a net source of $0.8 billion in 2000-01.

With a budgetary surplus of $8.9 billion and a net requirement of funds from non-budgetary transactions of $4.2 billion, there was a financial source, excluding foreign exchange transactions, of $4.7 billion in 2001-02, down from the financial source of $19.0 billion in 2000-01. This marks the sixth consecutive year in which a financial source has been recorded.

Among the major components of non-budgetary transactions:

- Loans, investments and advances were virtually unchanged, as the impact of borrowings for the Canada Student Loans Program was offset by repayments from Crown corporations and others.
- Pensions and other accounts recorded a net requirement of funds of $1.7 billion, compared to net source of $1.3 billion in 2000-01. The net requirement primarily reflects the reforms of the federal government employees' pension plans, effective April 1, 2000. Employer and employee contributions to the plans are now invested in financial markets, rather than being included as part of non-budgetary transactions. This reduces the non-budgetary source of funds by about $3 billion per year. In addition, a number of Crown corporations, which were members of the public sector pension plans, have set up their own pension plans, resulting in the transfer of the applicable assets to these new plans.
- Other transactions recorded a net requirement of $2.4 billion, compared to a net source of $2.2 billion in 2000-01. Developments in this component primarily reflect the conversion of accrual liabilities to cash. For example, in 2000-01 the federal government committed to providing the CFI with an additional $1.25 billion. This liability affected budgetary expenditures and therefore the budgetary balance in 2000-01, but had no impact on the financial balance, as the payment to the CFI was not made until June 2001. As a result, this liability resulted in a net source of funds in non-budgetary transactions in 2000-01 but a requirement for funds in 2001-02.

Financial requirements/source includes foreign exchange transactions. Foreign exchange transactions represent all transactions in international reserves held in the Exchange Fund Account (EFA). The objectives of the EFA are to provide general foreign currency liquidity for the Government and promote orderly conditions in the foreign exchange market. The EFA contains foreign currency investments, the Government's gold holdings and assets related to Canada's commitment to the International Monetary Fund (IMF). Increases in the level of reserves through borrowings, contributions to the IMF, and/or selling of Canadian dollars represent a requirement. Conversely, decreases in the level of reserves represent a source of funds. Taking all of these factors into account, there was a net requirement of $1.8 billion in 2001-02, compared to a net requirement of $8.8 billion in 2000-01.

As a result, there was a net financial source – the budgetary surplus plus non-budgetary and foreign exchange transactions – of $2.9 billion in 2001-02, compared to a net financial source of $10.2 billion in 2000-01.

With this net financial source and a drawing down of its cash balances, the Government retired $4.1 billion of its market debt. Cash balances at March 31, 2002, stood at $12.0 billion.

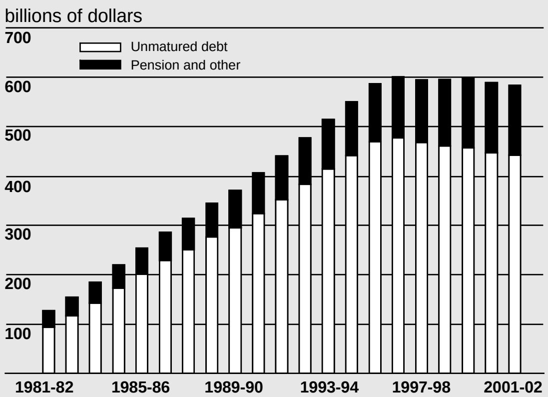
Total liabilities consist of interest-bearing debt and other liabilities. Interest-bearing debt includes unmatured, or market, debt and liabilities for pension and other accounts. At March 31, 2002, interest-bearing debt amounted to $583.4 billion, down $5.8 billion from the level a year earlier. Other liabilities, which include accounts payable and accrued liabilities, amounted to $40.7 billion, down $3.0 billion from 2000-01. As a result, total liabilities, or gross debt, stood at $624.1 billion.

Financial assets consist of cash and accounts receivable, foreign exchange accounts and loans, investments and advances. Capital assets, inventories and net receivables for tax revenues are not currently included, as capital assets and inventories are fully charged to expenditures at the time of acquisition or construction while tax revenues are reported on a cash basis. Financial assets totalled $87.6 billion at March 31, 2002, virtually unchanged from March 31, 2001.

As a result, net debt stood at $536.5 billion at March 31, 2002, down $8.9 billion from March 31, 2001, and $46.7 billion below the peak of $583.2 billion at March 31, 1997.

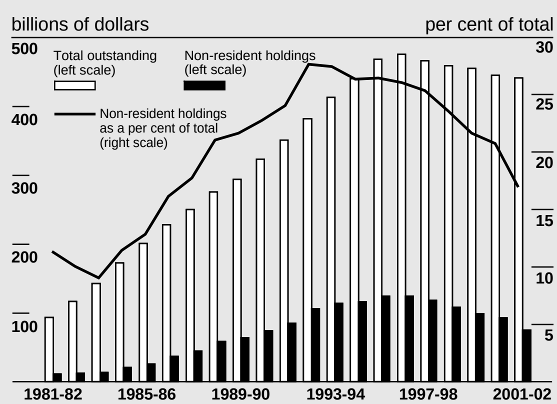
Foreign holdings of the Government of Canada's outstanding market debt are estimated at $75.1 billion at the end of March 2002. This represents 17 per cent of the Government's total market debt – the lowest ratio since 1986-87.

Interest-Bearing Debt



Source: *Public Accounts of Canada*.

Foreign Holdings of Government of Canada Market Debt



Source: Bank of Canada.

Table 6
Budgetary Balance and Financial Requirements/Source

	1997-98	1998-99	1999-00	2000-01	2001-02
			($ billions)		
Budgetary balance	3.8	3.1	12.7	18.1	8.9
Non-budgetary transactions					
Loans, investments and advances	1.6	0.3	-0.6	-2.7	-0.1
Pensions and other accounts					
Public sector pensions (net)	3.3	5.0	5.9	0.8	-2.3
Canada Pension Plan	0.5	1.2	0.8	0.2	0.4
Other	0.1	0.9	0.2	0.3	0.2
Total	3.8	7.0	7.0	1.3	-1.7
Other transactions	3.5	1.0	-4.5	2.2	-2.4
Total	8.9	8.4	1.9	0.8	-4.2
Financial requirements/source (excluding foreign exchange transactions)	12.7	11.5	14.6	19.0	4.7
Foreign exchange transactions	-2.2	-5.7	-6.8	-8.8	-1.8
Net financial balance	10.6	5.8	7.7	10.2	2.9
Net change in borrowings	-9.6	-6.9	-4.0	-10.0	-4.1
Change in cash balances	1.0	-1.1	3.7	0.2	-1.2
Cash in bank (March 31)	10.4	9.3	13.0	13.2	12.0

Table 7
Outstanding Debt at Year-End

	1997-98	1998-99	1999-00	2000-01	2001-02
			($ billions)		
Interest-bearing debt					
Unmatured debt	467.3	460.4	456.4	446.4	442.3
Pension and other accounts	127.5	134.6	141.5	142.8	141.2
Total	594.8	595.0	597.9	589.2	583.4
Other liabilities	43.7	45.3	40.7	43.6	40.7
Total liabilities (gross debt)	638.5	640.3	638.7	632.9	624.1
Financial assets	59.2	64.0	75.1	87.5	87.6
Accumulated deficit (net debt)	579.4	576.3	563.5	545.4	536.5

COMPARISON OF ACTUAL BUDGETARY OUTCOMES TO BUDGET ESTIMATES

This section compares the actual outcome for the major components of the budgetary balance for 2001-02 to the original estimates presented in the October 2000 *Economic Statement and Budget Update*, as well as to the updated estimates presented in the December 2001 budget.

The Government targeted a balanced budget for 2001-02 in both the October 2000 *Economic Statement and Budget Update* and December 2001 budget. Under the Debt Repayment Plan, the fiscal target for each year is based on:

- Using the average of private sector economic forecasts for budget-planning purposes.
- Including an annual Contingency Reserve to cover risks arising from unpredictable events and unavoidable inaccuracies in the economic and fiscal models used to translate the economic assumptions into detailed budget forecasts. It is not a source of funding for new policy initiatives. If not needed, it is used to reduce the public debt. For 2001-02 the Contingency Reserve was originally set at $3.0 billion. In the December 2001 budget, it was reduced to $1.5 billion to help cover some of the costs associated with the unforeseen circumstances of the global economic slowdown and the terrorist attacks of September 11th.
- Adding an extra degree of economic prudence to provide further assurance against falling back into deficit. In 2001-02 this economic prudence was originally set at $1 billion. In the December 2001 budget the Government used the economic prudence to manage the exceptional fiscal pressures resulting from the global economic slowdown and terrorist attacks.

Comparison to October 2000 *Economic Statement and Budget Update*

Economic growth for 2001 was significantly weaker than expected at the time of the October 2000 *Economic Statement and Budget Update*. Nominal income growth, based on the average of private sector forecasts, was projected at 5.5 per cent for 2001. However, the effects of the global economic slowdown in 2001 restrained the growth to 2.6 per cent, down considerably from the increase of 8.6 per cent reported for 2000.

In the October 2000 *Economic Statement and Budget Update*, before adjusting for the Contingency Reserve and economic prudence, there was an underlying surplus of $8.3 billion. After adjusting for the Contingency Reserve and economic prudence, there remained an unallocated balance of $4.3 billion, which the Government indicated could be directed to further debt reduction, increasing the prudence, further tax cuts or increased spending in priority areas.

The final outcome for 2001-02 was $8.9 billion, $0.6 billion higher than the underlying balance estimated in the October 2000 *Economic Statement and Budget Update*, as lower-than-expected public debt charges offset the impact of lower budgetary revenues and higher program spending (see Table 8). As a result, the prudence of $4.0 billion set aside in the *Economic Statement and Budget Update* was not required.

Table 8

Comparison of Actual Outcomes to October 2000 *Economic Statement and Budget Update*

	Actual	October 2000 *Economic Statement and Budget Update*	Difference
		($ billions)	
Budgetary revenues			
Personal income tax	83.8	80.5	3.3
Corporate income tax	24.0	28.6	-4.6
Other income tax	3.0	3.6	-0.5
Employment insurance premium revenues	18.0	18.4	-0.4
Excise taxes and duties	36.6	36.2	0.4
Non-tax revenue	7.9	7.2	0.6
Total	173.3	174.5	-1.2
Program spending			
Major transfers to persons			
Elderly benefits	25.4	25.2	0.2
Employment insurance benefits	13.7	12.2	1.5
Major transfers to other levels of government			
Canada Health and Social Transfer	17.3	17.3	0.0
Fiscal arrangements	12.0	12.5	-0.6
Alternative Payments for Standing Programs	-2.7	-2.5	-0.2
Direct program spending	60.9	59.9	1.1
Total	126.7	124.6	2.1
Public debt charges	37.7	41.7	-3.9
Underlying budgetary surplus	8.9	8.3	0.6
Prudence			
Contingency Reserve		3.0	-3.0
Economic prudence		1.0	-1.0
Total		4.0	-4.0
Budgetary outcome	8.9	4.3	4.6
Non-budgetary transactions	-4.2	-3.0	-1.2
Financial requirements/source (excluding foreign exchange transactions)[1]	4.7	-3.0	7.7

[1] In the *Economic Statement and Budget Update* a balanced budget was assumed for 2001-02.

Budgetary revenues were $1.2 billion lower than estimated in the October 2000 *Economic Statement and Budget Update*, primarily due to lower-than-expected corporate income tax revenues, which offset higher-than-expected personal income tax revenues. Personal income tax revenues were $3.3 billion higher, with about two-thirds due to higher payments on filing relating to the strong growth in net capital gains realizations in 2000, and the remainder due to prior-year adjustments. Corporate income taxes were $4.6 billion lower than forecast due to the weakness in global economic activity and its effect on corporate profits. Largely offsetting differences were reported among the other major components.

Program spending was $2.1 billion higher than estimated in the October 2000 *Economic Statement and Budget Update*. This primarily reflected higher EI benefits, due to the deterioration in the labour market in 2001, and increased direct program spending due to the new initiatives announced in the May 2001 *Economic Update* and December 2001 budget. In contrast, entitlements under fiscal arrangements were lower, reflecting the weakness in economic growth.

Public debt charges were $3.9 billion lower than forecast, reflecting the dramatic decline in short-term interest rates during 2001.

Comparison to December 2001 Budget

At the time of the December 2001 budget estimates indicated that the Canadian economy had contracted in the third quarter of 2001, and most forecasters were expecting further weakness in the fourth quarter, with only modest growth in the first half of 2002. Based on these economic planning assumptions and incorporating the impact of the budget initiatives, an underlying surplus of $1.5 billion was estimated. This amount was allocated to the Contingency Reserve.

However, stronger growth was recorded in the final quarter of 2001, and the recovery in the first half of 2002 was much faster and stronger than had been projected. As a result, budgetary revenues were higher than expected (up $2 billion – see Table 9). Most of this increase in budgetary revenues resulted from continued strength in personal income tax revenues (up $3.5 billion), as strong employment gains were recorded in the first quarter of 2002, and prior-year adjustments related to overpayments to the tax collection accounts.

Program spending was $3.9 billion lower than expected, reflecting lower-than-expected liabilities at year-end and a higher-than-assumed lapse in spending authority. The decline in public debt charges (down $1.5 billion) was attributable to lower-than-expected interest accrued on Canada Savings Bonds and pension account liabilities, reflecting the large declines in market interest rates.

Table 9

Comparison of Actual Outcomes to December 2001 Budget

	Actual	December 2001 budget	Difference
		($ billions)	
Budgetary revenues			
Personal income tax	83.8	80.3	3.5
Corporate income tax	24.0	23.6	0.4
Other income tax	3.0	4.0	-1.0
Employment insurance premium revenues	18.0	17.8	0.2
Excise taxes and duties	36.6	37.2	-0.6
Non-tax revenue	7.9	8.4	-0.5
Total	173.3	171.4	2.0
Program spending			
Major transfers to persons			
Elderly benefits	25.4	25.3	0.1
Employment insurance benefits	13.7	14.1	-0.4
Major transfers to other levels of government			
Canada Health and Social Transfer	17.3	17.3	0.0
Fiscal arrangements	12.0	12.2	-0.2
Alternative Payments for Standing Programs	-2.7	-2.4	-0.3
Direct program spending	60.9	64.1	-3.2
Total	126.7	130.6	-3.9
Public debt charges	37.7	39.2	-1.5
Underlying budgetary surplus	8.9	1.5	7.4
Prudence			
Contingency Reserve		1.5	-1.5
Economic prudence		0.0	0.0
Total		1.5	-1.5
Budgetary outcome	8.9	0.0	8.9
Non-budgetary transactions	-4.2	-1.9	-2.3
Financial requirements/source (excluding foreign exchange transactions)	4.7	-1.9	6.6

REPORT OF THE AUDITOR GENERAL ON THE CONDENSED FINANCIAL STATEMENTS OF THE GOVERNMENT OF CANADA

To the Minister of Finance:

The accompanying condensed statements of revenues, expenditures and accumulated deficit, assets and liabilities and changes in financial position are derived from the complete financial statements of the Government of Canada as at March 31, 2002, and for the year then ended on which I expressed an opinion without reservation in my Report to the House of Commons dated September 16, 2002.

My Report drew two matters I have raised before to Parliament's attention: a concern about the Employment Insurance Account, and the recording of transfers to Foundations. For more complete information, readers should refer to my Report, which will be included in Volume I of the *2002 Public Accounts of Canada*, expected to be tabled in the House of Commons later this year.

The fair summarization of the complete financial statements is the responsibility of the Government. My responsibility, in accordance with the applicable Assurance Guideline of The Canadian Institute of Chartered Accountants, is to report on the condensed financial statements.

In my opinion, the accompanying condensed financial statements fairly summarize, in all material respects, the related complete financial statements in accordance with the criteria described in the Guideline referred to above.

Since these are condensed financial statements, readers are cautioned that these statements may not be appropriate for their purposes. For more information on the Government's financial position, results of operations and changes in financial position, reference should be made to the related complete financial statements, which will also be included in Volume I of the *2002 Public Accounts of Canada*.

Sheila Fraser

Sheila Fraser, FCA
Auditor General of Canada

Ottawa, Canada
September 16, 2002

Condensed Financial Statements of the Government of Canada

The fundamental purpose of these condensed financial statements is to provide an overview of the financial affairs and resources for which the Government is responsible under authority granted by Parliament. Responsibility for the integrity and objectivity of these statements rests with the Government.

These financial statements are extracted and condensed from the audited financial statements included in Section 1 of Volume I of the *2002 Public Accounts of Canada*, which are expected to be tabled in Parliament later this year. As these condensed financial statements are, by their nature, summarized, they do not include all disclosure required for financial reporting by governments in Canada. Readers interested in the disclosure of more detailed data should refer to the audited financial statements in the Public Accounts.

Table 10

Government of Canada
Condensed Statement of Revenues, Expenditures and Accumulated Deficit for the Year Ended March 31, 2002

	2002	Restated 2001
	($ millions)	
Revenues		
Tax revenues		
Income tax	117,661	122,052
Other taxes and duties	39,602	39,017
Employment insurance premiums	17,980	18,731
	175,243	179,800
Non-tax revenues	12,224	13,550
Total gross revenues	*187,467*	*193,350*
Amounts deducted to arrive at net revenues	14,152	13,760
Total net revenues	*173,315*	*179,590*
Expenditures		
Transfer payments		
Old Age Security and related payments	24,632	23,667
Other levels of government	26,616	23,724
Employment insurance benefits	13,748	11,444
Other transfer payments	30,375	33,216
	95,371	92,051
Crown corporation expenditures	5,511	4,665
Other program expenditures	39,943	36,392
Total gross program expenditures	*140,825*	*133,108*
Amounts deducted to arrive at net program expenditures	14,152	13,760
Total net program expenditures	*126,673*	*119,348*
Interest on debt	37,735	42,094
Total net expenditures	*164,408*	*161,442*
Surplus for the year	8,907	18,148
Opening accumulated deficit as originally reported	547,378	564,526
Less: Adjustment to tax revenues (note 2)	1,982	982
Opening accumulated deficit as restated	545,396	563,544
Accumulated deficit at end of year	536,489	545,396

Table 11

Government of Canada
Condensed Statement of Assets and Liabilities
as at March 31, 2002

	2002	Restated 2001
	($ millions)	
Liabilities		
Payables, accruals and allowances		
Accounts payable and accruals	31,434	34,135
Allowances for guarantees and employee benefits	9,245	9,509
Total	40,679	43,644
Interest-bearing debt		
Unmatured debt		
Marketable bonds	293,843	294,973
Treasury bills	94,039	88,700
Canada savings and Canada premium bonds	23,966	26,099
Non-marketable bonds and notes	3,391	3,473
Total payable in Canadian currency	415,239	413,245
Payable in foreign currencies	27,032	33,158
Total	442,271	446,403
Pension and other accounts		
Public sector pensions	126,921	129,185
Due to Canada Pension Plan	6,770	6,391
Other	7,469	7,253
Total	141,160	142,829
Total interest-bearing debt	583,431	589,232
Total liabilities	*624,110*	*632,876*
Assets		
Cash and accounts receivable		
Cash	13,467	15,594
Accounts receivable	3,362	2,966
Total	16,829	18,560
Foreign exchange accounts	52,046	50,270
Loans, investments and advances		
Enterprise Crown corporations and other government business enterprises	9,192	10,085
National governments and international organizations	7,342	7,541
Other	11,283	10,203
Total	27,817	27,829
Less allowance for valuation	9,071	9,179
Total	18,746	18,650
Total assets	*87,621*	*87,480*
Accumulated deficit	*536,489*	*545,396*

Table 12

Government of Canada
Condensed Statement of Changes in Financial Position
for the Year Ended March 31, 2002

	2002	Restated 2001
	($ millions)	
Cash provided by operating activities		
Surplus for the year	8,907	18,148
Expenditures not requiring cash	9,301	5,194
	18,208	23,342
Net payments from pension and other accounts	(10,470)	(7,111)
Net change in receivables, payables and accruals	(4,006)	4,960
	3,732	21,191
Cash provided (used for) investing activities		
Net decrease (increase) in loans, investments and advances	49	(1,329)
Cash used for foreign exchange activities		
Net (decrease) increase in foreign currency borrowings	(6,126)	570
Net increase in foreign exchange accounts	(1,776)	(8,776)
	(7,902)	(8,206)
Net cash (required) generated before financing activities	*(4,121)*	*11,656*
Cash provided by (used for) financing activities		
Net increase (decrease) in Canadian currency borrowings	1,994	(10,573)
Net (decrease) increase in cash	(2,127)	1,083
Cash at beginning of year	15,594	14,511
Cash at end of year	*13,467*	*15,594*

Notes to the Condensed Financial Statements

1. Significant Accounting Policies

The Government of Canada reporting entity includes all departments, agencies, corporations and funds which are owned or controlled by the Government and which are accountable to Parliament. The financial activities of all these entities are consolidated in these statements, except for enterprise Crown corporations and other government business enterprises, which are not dependent on the Government for financing their activities. These corporations are reported as investments at their original cost adjusted by an allowance for valuation to reflect their annual profits or losses. The Canada Pension Plan is excluded from the reporting entity as it is under the joint control of the Government and participating provinces.

The Government basically accounts for transactions on an accrual basis. Two notable exceptions are tax revenues and related refunds, which are generally accounted for on a cash basis; and capital assets, which are fully charged to expenditures at the time of acquisition or construction.

As a consequence, the only assets recorded on the Condensed Statement of Assets and Liabilities are financial assets, as they can provide resources to discharge liabilities or finance future operations. Assets are recorded at the lower of cost or net realizable value. Liabilities are recorded on an accrual basis with public sector pension and severance liabilities being determined on an actuarial basis. Valuation allowances are established for loan guarantees, concessionary and sovereign loans, and other obligations.

Some amounts in these statements are based on estimates and assumptions made by the Government. By their nature, such estimates are subject to measurement uncertainty, although all of them are believed to be reasonable.

Comparative figures for 2001 have been reclassified to conform to the current year's presentation.

2. Overpayments Under Tax Collection Agreements

On September 4, 2002, the Government announced its decision to recover over a 10-year period beginning in fiscal year 2004-2005, approximately $1,421 million in overpayments to provinces related to mutual fund trust capital gain refunds applicable to the 1997 to 1999 tax years.

The misclassification of mutual fund trust capital gain refunds resulted in the understatement of tax revenues for fiscal years prior to 2001-2002. To reflect the increase in tax revenues resulting from the decision to recover $1,421 million in overpayments, $982 million on a present value basis, for fiscal years 1997-1998 to 1999-2000, the opening accumulated deficit as at March 31, 2000 has been decreased by $982 million. In addition, the financial statements for fiscal year 2000-2001 have been restated to reflect a $1,000 million increase in tax revenues due to the correction of the understatement of tax revenues for tax year 2000. The cumulative effect of these adjustments results in a decrease in the opening accumulated deficit as at March 31, 2001, of $1,982 million.

3. Reporting of Revenues and Expenditures on a Gross Basis

Detailed amounts on the Condensed Statement of Revenues, Expenditures and Accumulated Deficit are presented on a gross basis only. Gross revenues include revenues of consolidated Crown corporations, and revenues of government departments, agencies and funds which, on the net basis, are deducted from expenditures for budget and parliamentary authority purposes. Gross expenditures include expenditures determined through the tax system, such as child tax benefits and quarterly GST tax credits, that are deducted from revenues on the net basis.

4. Contractual Commitments

Contractual commitments that will materially affect the level of future expenditures include transfer payment agreements, benefit plans for veterans and others, capital asset acquisitions and other purchases, operating and capital leases, and funding of international organizations. At March 31, 2002, contractual commitments amounted to approximately $40 billion ($37 billion in 2001).

5. Contingent Liabilities

Contingent or potential liabilities that may become actual liabilities in future years include: guarantees by the Government; callable share capital in international organizations; claims and pending and threatened litigation; and environmental contingencies. Contingent liabilities related to guarantees by the Government and to international organizations amount to $77 billion ($72 billion in 2001). The total amount claimed against the Government for other claims and pending and threatened litigation is not determinable; however, there are over $200 billion in claims for Aboriginal and comprehensive land claims. The Government is confident that the ultimate settlement for these contingent liabilities will be for amounts significantly lower than those being disclosed.

Insurance in force relating to self-sustaining insurance programs operated for the Government by three enterprise Crown corporations amounted to approximately $615 billion ($586 billion in 2001). The Government expects that it will not incur any costs to cover the claims for these programs.

6. Changes in Accounting Policies

The Government had intended to change its basis of accounting from the current modified accrual basis to the full accrual basis for the preparation of these financial statements. Given the timing of the 2001 budget and the fact that important components of the information required to implement full accrual accounting had not yet been verified and audited, the Government decided to delay the implementation of full accrual accounting for at least one year.

Other Sources of Information

The Public Accounts of Canada

The *Public Accounts of Canada*, as required under section 64(1) of the Financial Administration Act, are tabled in the fall of each year by the President of the Treasury Board. This report is presented in two volumes:

- Volume I contains the Government's audited financial statements and supporting schedules and information; and
- Volume II contains details of financial operations by ministry (Part I) and additional information and analyses (Part II).

The Budget

The budget, usually introduced in February, presents the Government's overall fiscal plan, incorporating revenue projections and spending plans, which combine to determine the resulting budgetary balance. The budget also introduces proposals for changes in taxation.

The Fiscal Monitor

This monthly newsletter produced by the Department of Finance highlights the financial results of the Government together with the reasons underlying major variances.

Debt Management Strategy

This report is tabled annually in Parliament. It provides information on the federal government's debt management strategy for the coming fiscal year.

The Debt Management Report

This annual document provides an accounting of the key elements of federal debt strategy and describes various strategic and operational aspects of the Government's debt program and cash management activities over the past fiscal year.

The Estimates

Each year the Government prepares Estimates in support of its request to Parliament for authority to spend public monies. This request is formalized through the tabling of appropriation bills in Parliament. The Estimates are tabled in the House of Commons by the President of the Treasury Board and consists of three parts:

Part I – The Government Expenditure Plan provides an overview of federal spending and summarizes the relationship of the key elements of the Main Estimates to the Expenditure Plan set out in the budget.

Part II – The Main Estimates directly support the Appropriations Act.

Part III – Departmental Expenditure Plans, which consist of two components – Reports on Plans and Priorities and Departmental Performance Reports.