BALANCED BUDGET LEGISLATION: AN ASSESSMENT OF THE RECENT CANADIAN EXPERIENCE

Michael A. Geist[*]

During the past several years Canadian budgetary policy has focused on reining in government spending and reducing annual budget deficits and overall government debt. One response to the growing budgetary concerns has been a rising interest in balanced budget legislation. Today, half of Canada's provincial governments have balanced budget legislation in force or scheduled for adoption. Moreover, since 1991, seven provincial governments, one territory, and the federal government have enacted or tabled legislation that targets government spending and professes to have deficit reduction as a primary goal.

Notwithstanding the popularity of balanced budget legislation, there has been little, if any, analysis of the utility of such legislation in a Canadian context. This article seeks to fill this void by comparing differing approaches to balanced budget legislation and, by engaging in such a comparison and by drawing on the experiences and approaches in other jurisdictions, to determine whether balanced budget legislation is the veritable panacea its advocates suggest, the worthless endeavour its critics claim, or something in between these two extremes. Furthermore, using constitutional and public choice principles, the theoretical justifications for balanced budget legislation are explored and a

Ces dernières années, la politique budgétaire canadienne a surtout porté sur le contrôle des dépenses gouvernementales, la réduction des déficits budgétaires annuels et la diminution de l'ensemble de la dette publique. Pour dissiper les inquiétudes croissantes à l'égard des questions budgétaires, on s'intéresse de plus en plus aux lois sur l'équilibre budgétaire. Aujourd'hui, la moitié des gouvernements provinciaux du Canada ont une loi sur l'équilibre budgétaire qui est en vigueur ou prévue pour adoption. En outre, depuis 1991, sept gouvernements provinciaux, un territoire et le gouvernement fédéral ont promulgué ou présenté des lois qui s'attaquent aux dépenses gouvernementales et sont censées avoir comme but principal la réduction du déficit.

Malgré la popularité des lois sur l'équilibre budgétaire, on a peu analysé l'utilité de ces lois dans le contexte canadien, si tant est qu'on l'ait analysé. Le présent article vise à combler cette lacune grâce à une comparaison des différentes approches des lois sur l'équilibre budgétaire. En faisant cette comparaison et en s'inspirant de l'expérience et des approches des autres ressorts, l'auteur essaie de déterminer si les lois sur l'équilibre budgétaire sont la véritable panacée que ses partisans préconisent, l'entreprise inutile que ses détracteurs annoncent ou quelque chose se

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* Associate in Law, Columbia University School of Law. LL.B. 1992, Osgoode Hall Law School, York University; LL.M. 1994, Wolfson College, Cambridge University. A draft of this paper was presented to the 26th Annual Workshop on Commercial and Consumer Law in Toronto in October 1996. The author would like to express his thanks to the participants at the Workshop for their insightful comments; Jacob Ziegel and Vaughan Black for facilitating the author's participation; Peter Strauss, Rene Geist and several anonymous reviewers for their helpful feedback; the faculty of the Dalhousie Law School where the author conducted this research while an Assistant Professor of Law; the Canada-U.S. Fulbright Foundation, the Social Sciences and Humanities Research Council of Canada, and the Columbia Law School for their financial support; and Allison Geffen for her continued love and encouragement. Any errors or omissions, however, remain the sole responsibility of the author.

framework for assessing the legal and practical viability of such legislation in a Canadian context is developed.

The article concludes that there are some tangible benefits to be gained from balanced budget legislation, particularly with regard to increased political accountability. However, genuinely effective balanced budget legislation must incorporate a series of criteria in order to move beyond mere policy statements. These criteria include the inclusion of penalty provisions with effective consequences, reference in the legislation to both revenues and expenditures, flexibility with regard to budgetary periods and deficit targets, and increased clarity and disclosure of the budgetary process. Ultimately, however, deficit reduction and the maintenance of a balanced budget require political leadership; a quality that legislation, no matter how well drafted, does not guarantee.

situant entre ces deux extrêmes. En outre, l'auteur se fonde sur les principes constitutionnels et ceux relatifs aux choix publics pour examiner les justifications théoriques sur lesquelles reposent les lois sur l'équilibre budgétaire et élaborer un cadre d'évaluation de la viabilité de ces lois sur les plans pratique et juridique.

Enfin, l'auteur conclut que les lois sur l'équilibre budgétaire peuvent nous procurer des avantages réels, notamment une plus grande responsabilisation au niveau politique. Cependant, pour être vraiment efficaces, les lois sur l'équilibre budgétaire doivent renfermer une série de critères afin d'être plus que de simples énoncés de principes. Ces critères comprennent des dispositions punitives ayant des conséquences effectives, une mention dans la loi concernant les recettes et les dépenses, de la flexibilité en ce qui a trait aux périodes budgétaires et aux objectifs à atteindre sur le plan du déficit, une plus grande précision et la divulgation du processus budgétaire. Mais en définitive, la réduction du déficit et le maintien d'un budget équilibré nécessitent un leadership politique, qualité qui n'est pas garantie par les lois, qu'elles soient bien rédigées ou non.

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I. INTRODUCTION

"[T]his is a Bill that stands for balanced budgets, balanced budgets forever"

—Alberta Treasurer Dinning moving the second reading of Alberta's *Balanced Budget and Debt Retirement Act*, March 1995[1]

During the past several years Canadian budgetary policy, at both the federal and provincial levels, focused primarily, if not obsessively, on reining in government spending and reducing annual budget deficits and overall government debt.[2] In the process, Canadians have grown accustomed to reports of an ever-increasing national debt,[3] slogans such as "mortgaging our future", and warnings that failure to reverse the present course will result in, among other things, higher interest rates and a greater dependence upon foreign capital.[4]

One response to the growing budgetary concerns has been a rising interest in balanced budget legislation.[5] Politicians,[6] media,[7] government analysts,[8] the finance

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[1] *Alberta Hansard* No. 24 (13 March 1995) at 516.

[2] For a good historical examination of Canada's ongoing budgetary concerns, see J.P. Feehan, "The Federal Debt" in S.D. Phillips, ed., *How Ottawa Spends 1995-96: Mid-Life Crises* (Ottawa: Carleton University Press, 1995) 31 [hereinafter Feehan].

[3] Although Canada had a significant national debt following World War II, it was actually able to run a budgetary surplus for much of the early 1950s as the debt was reduced to more manageable levels. From the mid-1960s until the first oil shock in 1973, Canada ran budget deficits of just under one percent of GDP. Moreover, with the economy continuing to expand, the federal debt-to-GDP ratio declined during the early 1970s.

In 1975, the federal government introduced automatic indexation to transfer payments and personal income tax. This increased commitment to social programs came at a time when the economy was also experiencing a severe recession following the oil shock. As a result, the federal debt steadily increased so that by 1979 the federal *deficit* was 3 1/2 times larger than the total *budget* in 1951. The power of compounding took over during the 1980s and 1990s with the debt increasing over seven times from the already significant figure in 1979. T. Carmichael, "Background Paper — A Personal Reflection on Deficits and Debt" in Office of the Auditor General of Canada, *Deficits and Debt: Proceedings of the Colloquium* (Ottawa: 1993) 27.

Today, as a result of 25 consecutive years of deficit financing, the federal debt stands at over $545 billion and, notwithstanding attempts to reduce the national deficit, continues to rise. Department of Finance, *The Economic and Fiscal Update* (Ottawa: 6 December 1995) at 29 [hereinafter *Fiscal Update*].

[4] There is not, however, universal agreement on the extent to which the deficit is damaging nor on its impact to the Canadian economy. There are those who contend that claims regarding the harm inflicted by the debt are exaggerated and that deficit reduction is actually used primarily as a means of effecting social policies such as eliminating social programs. See, *e.g.*, J. Loxley, "Balanced Budget Legislation or Bad Budget Legislation?" *Canadian Dimension* (1 December 1995) 19.

Conversely, there are commentators who argue that the current situation is far worse than is generally perceived. For example, Robin Richardson points out that when unfunded liabilities such as the Canada Pension Plan (CPP) are added to the national debt figure, the debt-to-GDP ratio nearly doubles. Feehan, *supra* note 2 at 38-9.

[5] Although balanced budget legislation may be new to Canada and derided by some as a "fad", it has been a budgetary consideration for a considerable period of time. In fact, in modern times its rise as a serious fiscal consideration coincided with the introduction of the modern

community[9] and public interest groups[10] have suggested that the ongoing struggle to reduce the deficit is ample evidence of governments' structural inability to behave in

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budgetary process of government preparing periodic estimates of anticipated expenses and submitting such estimates to legislatures for approval and authorization of funding. For an interesting look at the historical origins of balanced budget legislation, see, C.C. Webber, "Development of Ideas about Balanced Budgets" in A. Wildavsky, *How To Limit Government Spending* (Berkeley: University of California Press, 1980) 163. See also S.E. Sterk and E.S. Goldman, "Controlling Legislative Shortsightedness: The Effectiveness of Constitutional Debt Limitations" (1991) 6 Wisc. L. Rev. 1301.

[6] There are presently six balanced budget statutes in force or tabled in Canada. In addition, during the election campaign of 1995, then candidate (now Premier of Ontario) Mike Harris pledged that "[c]ertainly within our first term of office...we intend to pass meaningful legislation to prevent any future governments from running deficits." R. Brennan, "Grits, Tories Urge Deficit Bar" *The [Windsor] Star* (4 April 1995) A8 [hereinafter Brennan].Note, however, that there has not been unanimous acceptance of the balanced budget legislative approach. For example, Paul Martin, the current federal finance minister has steadfastly refused to adopt such an approach arguing that balanced budget legislation limits the choices available to duly elected governments and encourages "ingenious politicians and bureaucrats to spend time looking for ways to get around the rules through accounting hocus-pocus and subterfuges of various kinds." R. Carrick, "Balanced Budget Legislation Draws Criticism from Martin" *The [Windsor] Star* (2 September 1995) H8.

Furthermore, some analysts argue that legislative rules are unnecessary given the power of the financial markets to exert influence over government policy. See, *e.g.,* R.D. Kneebone, "Deficits and Debt in Canada: Some Lessons from Recent History" (1994) 20 Can. Pub. Pol. 152. However, Marcel Côté takes the opposite approach, arguing that "[d]espite all the rhetoric, financial markets are not reliable allies: they make too much of their living selling government debt..." M. Côté, "Coping with the Canadian Public Debt Crisis" in Office of the Auditor General of Canada, *Deficits and Debt: Proceedings of the Colloquium* (Ottawa, 1993) 9 at 14 [hereinafter Côté].

[7] See, *e.g.*, "Martin Should Put it in Writing" *The Financial Post* (16 January 1996) 16; D. Francis, "The Most Serious Threat Our Nation Faces is the Debt" *The Financial Post* (6 April 1996) 21; R. Scowen, "It's Time for Quebec to Have its Own Balanced-Budget Legislation" *[The Montreal] Gazette* (25 March 1995) C3.

[8] Library of Parliament Research Branch, *Fiscal Rules for the Control of Government* (Background Paper 358E) by M.G. Wrobel (Ottawa: November 1993).

[9] For example, the chief economist of the Royal Bank recently called for the enactment of legislation mandating balanced budgets. G. McIntosh, "Bank Wants Legislation to Balance Budgets" *The [Ottawa] Citizen* (28 February 1997) D8.

[10] For example, in a 1995 study, Robin Richardson of the Fraser Institute argued for "debt-elimination laws for all levels of government." N. Nankivell, "Should Ottawa Now Consider Legislated Debt Reduction?" *The Financial Post* (7 October 1995) 20. Similarly, in a study published by the C.D. Howe Institute, Herbert G. Grubel argued for a *constitutional* amendment mandating a balanced budget at the federal level. H.G. Grubel, "Constitutional Limits on Government Spending Deficits and Levels in Canada" in H.G. Grubel, D.D. Purvis, and W.M. Scarth, *Limits to Government: Controlling Deficits and Debt in Canada* (Winnipeg: C.D. Howe Institute, 1992) 1.

Furthermore, the Canadian Taxpayers' Federation, a national organization concerned with "tax fairness" issues, has also joined the call for balanced budget legislation arguing that "[w]ithout a comprehensive law which includes strict enforcement mechanisms and financial penalties against politicians who break their commitments, targets and plans...are worthless." T. Lanigan, "A Law to Limit B.C. Politicians' Tax and Spend Powers" *The [Vancouver] Sun* (22 November 1995) A19.

what is perceived to be a "fiscally prudent" manner. Furthermore, the public has become skeptical of long-term debt reduction plans, noting that legislative inertia and a "pass the buck" mentality often pervades the House of Commons and provincial legislatures.[11] As a result, legally mandated deficit reduction and balanced budget requirements are frequently viewed as the only viable solutions to an otherwise intractable problem.

As a consequence of this public pressure, half of Canada's provincial governments now have balanced budget legislation in force.[12] In fact, since 1991, seven provincial governments, one territory, and the federal government have enacted legislation that targets government spending and professes to have deficit reduction as a primary goal.[13] Of the four remaining provinces and territories, the Harris government in Ontario has pledged to enact balanced budget legislation during its first term in office,[14] leaving Newfoundland, Prince Edward Island and the Yukon as the only Canadian jurisdictions not to have experimented with some form of balanced budget legislation during the 1990s.

Notwithstanding the popularity of balanced budget legislation, there has been little, if any, analysis of the utility of such legislation in a Canadian context beyond the headline producing arguments noted above.[15] Moreover, the enacted or proposed legislation varies widely across provinces. Close scrutiny reveals that statutory provisions pertaining to budgetary periods and expenditures covered, penalty provisions, amending formulae, budgetary disclosure, and accounting practices are far from uniform. Accordingly, though there may be significant agreement on the need for some form of legislation, there is no agreement on an ideal approach.

This article seeks to fill this void by assessing the recent Canadian balanced budget legislative experience. It should be noted that the examination of balanced budget legislation should not be regarded as an unqualified endorsement of balanced budgets *per se*. In fact, there are compelling arguments that assert that there is nothing "magical" about balanced budgets and that maintaining a deficit may in some instances be beneficial or, at a minimum, not particularly harmful.[16] Rather than engage in a debate on the merits of balanced budgets, however, the scope of the article is limited to establishing a constitutional and public choice paradigm to assess the effectiveness of

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[11] Côté, *supra* note 6.

[12] Alberta, Manitoba, New Brunswick, Saskatchewan, Québec and the Northwest Territories have enacted balanced budget legislation.

[13] Alberta and Nova Scotia enacted spending limitation legislation.

[14] Brennan, *supra* note 6.

[15] One notable exception is a recent article by Professor Lisa Philipps who argues that the rise of balanced budget legislation in Canada represents dangers to economic stability, social justice, and political democracy. L.C. Philips, "The Rise of Balanced Budget Laws in Canada: Legislating Fiscal (Ir)Responsibility" (1996) 34 Osgoode Hall L.J. 681.

As discussed in Part IV, there has been considerable analysis and discussion of balanced budget legislation in the United States, however, where a constitutional balanced budget amendment has numerous advocates and where some form of balanced budget legislation is common at the state level. Given the differences between the Canadian parliamentary system and the U.S. system, as well as the differences in budgetary processes, U.S. analysis is not entirely applicable in a Canadian context.

[16] A. Effinger, "Do Deficits Matter?: Many Nations Yet to Reap Rewards of Fiscal Prudence" *The [Montreal] Gazette* (31 October 1996) D2.

Canadian balanced budget legislation.

Since much of the legislation in question is new and has not had an adequate opportunity to fully impact on government spending practices, this assessment, with several exceptions, does not focus on actual deficit reduction. In fact, given the recent success of several provinces in reaching a balanced budget status, the true test of the effectiveness of Canadian balanced budget legislation is only likely to arise in several years, when the cyclical nature of economies yields new budgetary pressures that may force politicians to engage in significant cuts, creative accounting, legislative amendment, or some combination thereof.[17] Leaving aside the most recent spending practices of Canadian governments, the article endeavours to compare differing approaches and, by engaging in such a comparison and by drawing on the experiences and approaches in other jurisdictions, determine whether balanced budget legislation is the veritable panacea its advocates suggest,[18] the worthless endeavour its critics claim,[19] or something in between these two extremes.

Following this introductory portion of the article, Part II develops an analytical paradigm to assist in the normative analysis of the eleven different balanced budget statutes that have been enacted in Canada since 1991.[20] Using constitutional and public choice principles, the article explores the theoretical justifications for balanced budget legislation are explored and develops a framework for assessing the legal and practical viability of such legislation in a Canadian context is developed.

Part III of the article examines the eleven different balanced budget statutes that have been enacted or tabled in Canada since 1991. For the purposes of this article, both legislation that prescribes limits to government spending and legislation that mandates a balanced budget are included. Although the former may not be strictly balanced budget legislation, in view of the similar goals encompassed by such legislation, they are worthy of examination within the balanced budget legislation context.[21]

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[17] Several Canadian provinces, including Alberta, Saskatchewan, Newfoundland, Prince Edward Island, New Brunswick, Manitoba and British Columbia, have balanced, or claim to have balanced their budgets for the 1996 or 1997 fiscal periods. Given the newness of balanced budget legislation, the extent to which it may have impacted on the provinces' fiscal performance is difficult to gauge. D. Martin, "Hallelujah!: The Deficit is Dead" *Calgary Herald* (22 February 1996) A15.

[18] Then-Premier Vander Zalm proclaimed that B.C.'s version of a balanced budget statute was "the greatest achievement by any government in this province's history or this country's history." *British Columbia Debates of the Legislative Assembly,* No. 21 (23 May 1991) at 12162.

[19] In debating Alberta's first foray into balanced budget legislation, one opposition MLA described the legislation as "a Bill that accomplishes nothing." Alberta, Legislative Assembly of Alberta, *Alberta Hansard* at 1620 (24 June 1992) [hereinafter Mitchell].

[20] The eleven include three separate pieces of legislation enacted by Alberta, legislation enacted by the federal government and by governments in British Columbia, Saskatchewan, Manitoba, Nova Scotia, New Brunswick, and the Northwest Territories, and legislation tabled but not yet enacted in Quebec.

[21] For example, although the Nova Scotia legislation is better characterized as spending control legislation, when introduced, the government suggested that the legislation was, in fact, balanced budget legislation. S. Thorne, "N.S. Promises Law to Balance Budgets" *The Financial Post* (7 April 1993) 6.

Furthermore, some of the statutes in question also regulate issues such as tax increases and debt retirement. However, this article assesses only those provisions pertaining to government spending and deficit reduction.

The eleven statutes, which are categorized as either spending limitation legislation or balanced budget legislation, are canvassed in chronological order so that the Canadian development of such legislation can be more easily identified. Each piece of legislation is examined on the basis of the following substantive criteria:

1. Enumerated goals of the statute and timing of enactment;
2. Budgetary period covered (*ie.* one year, two years, etc.);
3. Governmental spending covered (*ie.* program spending, capital expenditures, etc.);
4. Existence of penalty provisions;
5. Existence of an amending formula;
6. Existence of provisions mandating increased clarity and disclosure of budgetary targets and deficit reduction progress.

Part IV of the article provides a limited comparison of the balanced budget legislation approaches in other jurisdictions. Although a comprehensive analysis is beyond the scope of this article, this discussion endeavours to familiarize the reader with activities in the United States, the European Union, and New Zealand, since their experiences may provide valuable lessons in the assessment of the Canadian experience.

Part V draws on the previous discussion by providing recommendations for Canadian jurisdictions and assessing which of the current statutes may have the most beneficial impact. The article concludes that somewhere between the rhetoric of balanced budget legislation's advocates and critics, there are some tangible benefits particularly with regard to increased political accountability. However, genuinely effective balanced budget legislation must incorporate a series of criteria in order to move beyond mere policy statements. These criteria include inclusion of penalty provisions with effective consequences, reference in the legislation to both revenues and expenditures, flexibility with regard to budgetary periods and deficit targets, and increased clarity and disclosure of the budgetary process.

Ultimately however, the article concludes that deficit reduction and the maintenance of a balanced budget requires political leadership; a quality that legislation, no matter how well drafted, does not guarantee. Therefore, although there may be a place for balanced budget legislation in Canada, its benefits are far more limited than its proponents claim. Moreover, most Canadian balanced budget legislation fails to meet all the criteria referenced above and, as such, is likely to have only minimal, if any, impact on the movement toward increased fiscal discipline in Canada.

II. AN ANALYTICAL PARADIGM OF BALANCED BUDGET LEGISLATION

Although economists, political scientists, and legal academics have devoted considerable energy to the issue of balanced budget legislation in the United States,[22] the relative newness of such legislation in Canada has resulted in a dearth of analysis from a Canadian perspective. Accordingly, this section of the article uses constitutional and public choice theories to explain why balanced budget legislation can be perceived to be a rational and effective course of conduct, with particular application to the

[22] For references to numerous works on the topic, see *infra*, Part IV.A.

Canadian context.[23]

When viewed at its most general level, balanced budget legislation is an attempt by government to bind itself. By enacting such legislation, government precommits itself to a particular course of action. Precommitment is a more common practice than is often perceived as Jon Lester noted in his seminal work on the topic, *Ulysses and the Sirens*:

> In modern democracies a number of institutions can be interpreted as devices for precommitment...the central bank can be seen as the repository of reason against the short-term claim of passion...Other institutions that have been accorded similar autonomy...include the Foreign Ministries of many countries and the BBC model of broadcasting...For these institutions it is possible to identify, with varying degrees of precision, the act of abdication whereby politicians have decided that certain values are too important, or certain tools too dangerous, to be subject to the current control of the politicians. The removal of monetary policy, foreign policy or broadcasting from the political sphere is itself a political act.[24]

Precommitment is not limited to institution building, however. In fact, the most common form of precommitment is the creation of a constitution. The development of a constitutional framework enables a single constituent assembly to lay down the ground rules for all future assemblies. Although these ground rules can be changed, this precommitment strategy is made effective by preventing easy amendment of the constitution.

The use of precommitments by government presents a paradox expressed effectively by Elster as "each generation wants to be free to bind its successors, while not being bound by its predecessors".[25] The critical issue that arises out of this paradox has important implications for balanced budget legislation - namely, insofar as precommitment hinders the ability of future governments to act in whatever manner they see fit, is precommitment anti-democratic? Applied to the balanced budget legislation context, the question is best framed as whether a government has the right to encumber future governments with specific spending criteria or procedures.

It is submitted that although precommitment can be anti-democratic, it can also enhance democracy. A society without any rules might be seen as completely free but such a society would also face the significant limitations that arise from the absence of any legal rules and structures. As Stephen Holmes notes:

> A preceding generation cannot prevent a succeeding generation from saying: "No more freedom!". But this incapacity does not imply that predecessors have no right or reason to design institutions with an eye to making such decisions difficult. When attempting to bind the future, constitutional-makers are not simply trying to exercise domination and control. Precommitment is justified because, rather than merely foreclosing

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[23] Although this part is limited to constitutional and public choice rationales for balanced budget legislation, other normative arguments, such as the need for institutional responsibility, intergenerational equity and economic prudence could also be raised. For further details on these arguments, see T. P. Seto, "Drafting a Federal Balanced Budget Amendment That Does What It Is Supposed To Do (And No More)" (1997) 106 Yale L.J. 1449.

[24] J. Elster, *Ulysses and the Sirens* (Cambridge: University Press, 1979) at 90.

[25] *Ibid.* at 94.

> options, it makes available possibilities which would otherwise lie beyond reach.[26]

Accordingly, just as framers of constitutions strive to create enduring democratic systems by limiting the power of any given majority[27] balanced budget legislation can similarly provide future governments with maximum fiscal power by limiting everyone's fiscal power to a limited extent. Viewed from this perspective, balanced budget legislation that clearly enumerates its objectives as providing for the long-term fiscal health of the country or province is not strictly a negative device that limits the powers of governments. Rather, such legislation can also be seen as a creative device that generates new fiscal possibilities by assigning fiscal powers and regulating the way in which those powers are exercised.

Canadian constitutional jurisprudence has grappled with the paradox presented by precommitments and developed a framework under which legislation can be assessed. The starting point for such analysis is the doctrine of parliamentary sovereignty which provides that Parliament or a Legislature may, acting within its sphere of competence, promulgate any new law or repeal any old laws. The power to alter old laws remains constant even in the face of an old law declared to be unamendable.[28] Such power is considered essential in order to ensure that a government in office is unable to frustrate the policies of future governments.

The power of Parliament to amend or repeal old laws is confirmed by both statute and case law. At the statutory level, s. 42(1) of the *Interpretation Act* provides that:

> Every Act shall be so construed as to reserve to Parliament the power of repealing or amending it, and of revoking, restricting, or modifying any power, privilege or advantage thereby vested in or granted to any person.[29]

The 1991 Supreme Court case of *Reference Re Canada Assistance Plan* demonstrates the Court's support of this doctrine.[30] The CAP Reference required the Court to rule on Parliament's power to enact legislation authorizing it to amend agreements between the federal government and the provinces. In this particular case, the federal government enacted legislation that effectively cut its contributions to the B.C., Alberta, and Ontario governments as part of an attempt to reduce the federal deficit. Sopinka J., speaking for a unanimous court, ruled that on the basis of parliamentary sovereignty, a government could not bind Parliament from exercising its powers to legislate amendments to the initial CAP agreement. Therefore, notwithstanding the existence of agreements between the federal government and the provinces which provided for amendment only upon the acquiescence of both parties, those agreements were incapable of limiting the power of Parliament to act as it saw fit.

Although it is clear that a government cannot bind Parliament, the issue with respect to balanced budget legislation is whether a Parliament can bind a future

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[26] S. Holmes, "Precommitment and the Paradox of Democracy" in J. Elster and R. Slagstad, eds., *Constitutionalism and Democracy* (Cambridge: University Press, 1988) 195 at 226.

[27] *Ibid.*

[28] P.W. Hogg, *Constitutional Law Of Canada*, 3rd ed. (Toronto: Carswell, 1992) at 307 [hereinafter Hogg].

[29] R.S.C. 1985, c. I-21.

[30] *Reference Re Canada Assistance Plan*, [1991] 2 S.C.R. 525, (1991) 83 D.L.R. (4th) 297 [hereinafter *CAP Reference*].

Parliament. The doctrine of parliamentary sovereignty makes clear that Parliament cannot bind future Parliaments with regard to the content, substance or policy of legislation.[31] However, the case law does suggest Parliament can bind future Parliaments with regard to procedural matters, commonly referred to as "manner and form" requirements.[32] The CAP Reference affirmed the as Sopinka J. noted:

> The argument is based on the idea that even a sovereign body can restrict itself in respect of the "manner and form" of subsequent legislation...In order for this argument to succeed, it would first have to be shown that Parliament intended, in the face of s. 42(1), to bind itself or to restrict the legislative powers of those of its members who are also members of the executive...It is no coincidence that when this court has found "manner and form" restrictions, the instrument creating the restrictions has not been an ordinary statute...It may be that where a statute is of a constitutional nature and governs legislation generally, rather than dealing with a specific statute, it can impose requirements as to manner and form. But where a statute has no constitutional nature, it will be very unlikely to evidence an intention of the legislative body to bind itself in the future.[33]

Accordingly, the Court will uphold as constitutional legislation that addresses the future action of the legislative body and is confined to procedural issues.[34]

Applied to balanced budget legislation, the Canadian constitutional jurisprudence presents several possibilities. First, it remains clear that certain elements of balanced budget legislation, particularly substantive provisions, cannot bind future governments. Therefore, notwithstanding claims to the contrary, balanced budget legislation is generally capable of amendment by future governments. However, certain elements within such legislation may be unamendable if its provisions are construed as manner and form requirements and evidence the intent to bind future governments. This exception has the potential to play a significant role in balanced budget legislation since the intent to be bound is often made plain within the statute and certain provisions, such as "supermajority" voting or budgetary disclosure requirements, could be interpreted as manner and form requirements. In view of the position of Canadian constitutional law, any assessment of Canadian balanced budget legislation must include an analysis of both the intent of the Parliament or Legislature and an assessment as to whether any provisions within the legislation might be construed as manner and form requirements. Although the above analysis demonstrates that balanced budget legislation

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[31] *Ibid.* at 324.

[32] For recent analysis of manner and form requirements, see R. Elliot, "Rethinking Manner and Form: From Parliamentary Sovereignty to Constitutional Values" (1991) 29 Osgoode Hall L.J. 215; K. Swinton, "Challenging the Validity of an Act of Parliament: The Effect of Enrolment and Parliamentary Privilege" (1976) 14 Osgoode Hall L.J. 345; and W.E. Conklin, "Pickin and Its Applicability to Canada" (1975) 25 U.T.L.J. 193.

[33] *CAP Reference*, *supra* note 30 at 322-23.

[34] However, Professor Hogg notes that even where a statutory provision looks like a manner and form restriction, it may in fact be one of four other kinds of laws. These include a provision that restricts the substance of future legislation, which is ineffective; a provision that is "directory" rather than "mandatory"; a provision that is regarded as a rule of interpretation, which would be displaced by any clear statutory indication to the contrary; and a provision that is regarded as an "internal" rule of parliamentary procedure, which would not invalidate another statute. Hogg, *supra* note 28 at 313-14.

is supportable from both democratic and constitutional perspectives, the desirability and effectiveness of such legislation must also be examined. Public choice theory, which takes an economic interest approach to political decision making is most helpful in this regard. In fact, public choice theory provides several bases for supporting the enactment of balanced budget legislation and for determining what provisions should maximize the legislation's effectiveness.

Public choice theory has provided several ways of examining government. The most common view of government that arises out of the public choice analysis is that governments act on the basis of maximizing popular support. Accordingly, governments formulate policies in order to win elections, rather than win elections to formulate policies.[35] Furthermore, this view of government maintains that macroeconomic variables directly impact on the popularity of government - that is, the better a country is performing economically, the more popular the government.[36] Under this model, the temptation for vote-seeking politicians to incur deficits by reducing taxes and/or increasing public spending is overwhelming given the direct correlation between the public's economic contentment and the politicians' re-election.

The model of government as a rational, vote-seeking body has considerable impact on balanced budget legislation analysis since it suggests that incurring deficits is often rational behavior. In order to prevent such behaviour from transpiring, constraints, such as balanced budget legislation, are necessary. Furthermore, the implications of this model suggest that balanced budget legislation may be appropriate even when the public stridently opposes deficit spending. For example, during the nineteenth century, the United States public viewed running a deficit in the United States virtually as an immoral act. Politicians rarely violated this norm since opposition parties were always eager to bring any excess government spending to the public's attention.[37] Under these circumstances, the rational course of action for government is to promote its fiscal rectitude, by, for example, enacting balanced budget legislation.

Although the vote-maximizing model often leads to calls for balanced budget legislation, it also provides several important lessons for the analysis of such legislation. First, given politicians proclivity to "go where the votes are", balanced budget legislation must be sufficiently flexible to ensure that adherence to its provisions remain a rational course of action under differing economic circumstances. Since government will adopt policies to gain votes, where the cost of compliance is greater than non-compliance, government will amend or simply disregard balanced budget legislation. This may occur during economic slowdowns when deficit spending may be viewed as an appropriate course of action, notwithstanding a general aversion to such activities. Accordingly, balanced budget legislation must contain sufficient incentives to make compliance attractive, but not be so inflexible as to leave government with no rational alternative but to disobey the law.

Second, since the adoption of balanced budget legislation may, in some circumstances, itself be a means of vote maximization (where the electorate favours such policies), an assessment of the "realpolitik" behind the legislation is needed. For example, where such legislation is enacted immediately prior to an election campaign,

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[35] D. C. Mueller, *Public Choice II* (Cambridge: University Press, 1989) at 179 [hereinafter Mueller].

[36] *Ibid.* at 294.

[37] *Ibid.* at 295.

the enactment is likely a means of currying support of the electorate rather than a genuine or bona fide attempt at deficit reduction. Conversely, where such legislation is enacted at the beginning of a government's term in office, the legislation may well represent a bona fide attempt to reduce the deficit. An illustration of realpolitik behind deficit reduction occured in British Columbia in 1996 when the governing New Democratic Party made a pre-election claim that it had balanced the budget. Following its reelection, a deficit approaching $1 billion dollars was discovered, ostensibly due to a "statistical error".[38]

A more radical view of government, advocated by Geoffrey Brennan and James Buchanan is to view government as Leviathan - that is, a monopolist that does not respond to political competition owing to the rational ignorance of voters, the uncertainties inherent in majority rule cycling, and collusion among elected officials.[39] Under this model, the desire of government to expand cannot be constrained merely by political competition and, therefore requires constitutional limitations on the power of government to tax and incur debt. This model of government clearly envisions a government that is beyond the reach of ordinary citizenry, constrained only by those constitutional provisions enacted at the state's inception.[40] At this extreme view of government, even balanced budget legislation is insufficient as constitutional entrenchment is a necessary prerequisite for effectiveness. Nevertheless, government as Leviathan provides a strong rationale for, at a minimum, effective balanced budget legislation that constrains government by employing penalty provisions, compliance incentives, and stringent deficit targets.

Finally, the public choice view of the electorate also has implications for balanced budget legislation. Public choice theorists point out that most voters are "rationally ignorant". Voters remain underinformed about political issues since the acquisition of such information is often costly to the individual voter, particularly given the fact that each individual's vote has a negligible impact on the outcome of an election. Since rational voters realize this, they do not expend time and money gathering information about the issues.[41] However, effective balanced budget legislation has the power to educate the electorate about deficit reduction by freely and regularly distributing information regarding government revenues and expenditures. Therefore, by mandating regular disclosure of government finances, balanced budget legislation may result in a better informed electorate.

The constitutional and public choice analysis demonstrate that balanced budget legislation has the potential to simultaneously enhance the democratic process, adhere to constitutional norms, and provide an effective means of constraining government fiscal policies. The analytical framework that arises out of this analysis suggests that balanced budget legislation can and should be assessed on several grounds. These include: an analysis as to whether the legislation clearly enunciates its goals; whether the legislation conforms with Canadian constitutional law, and, more particularly, whether certain provisions meet the manner and form exception; whether the legislation is sufficiently flexible to ensure compliance; whether the legislation contains penalty

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[38] A. Coyne, "Bouchard, Clark Forced to Eat Their Words on Deficit Cuts; Politicians Caught in a Lie a Poignant Sight" *[Edmonton] Journal* (2 November 1996) A15.

[39] Mueller, *supra* note 35 at 268.

[40] *Ibid.* at 270.

[41] *Ibid.* at 206.

provisions to encourage compliance; whether, having regard to the timing of its enactment, the legislation appears to be a bona fide attempt to constrain fiscal policies; and whether the legislation enhances the electorate's understanding of the issues by increasing the amount of information available to the public at-large. The next section utilizes this analytical framework to assess the eleven balanced budget statutes that have been enacted or tabled in Canada in the 1990s.

III. BALANCED BUDGET LEGISLATION IN CANADA

The widespread adoption of balanced budget legislation in Canada in the 1990s has not produced much uniformity in the actual provisions of the different statutes. The differing approaches are particularly striking in view of the fact that the goals of the various pieces of legislation, as professed in the legislative debates and in the media, are largely the same. Moreover, a brief review of both the governments' claims regarding the "historical nature" of the legislation and the oppositions' denigration of the legislation as little more than a public relations exercise, leaves the distinct impression that the drafters of each statute (and its commentators) have neglected to engage in much "comparison shopping".

A. *Spending Control Legislation*

1. Spending Control Act[42] *(Federal)*

The first two attempts at legislated deficit reduction occurred in 1991; the first in March of that year at the provincial level by the Social Credit government in British Columbia and the second at the federal level by the Progressive Conservative government in Ottawa.

As part of its 1991 budget, the federal government announced several measures designed to directly control spending and to indirectly limit the growth of the federal debt. Among these measures was the adoption of the SCA, an Act whose aims were to control program spending, increase budgetary disclosure and provide flexibility in the event of an economic downturn.

Rather than control all federal government spending, the SCA's ambitions were far more modest. The statute established ceilings, or caps, to program spending. Program spending was defined as all expenditures other than, among other things, costs associated with servicing or repayment of the debt, *Unemployment Insurance Act*[43] expenditures, and expenditures incurred as a direct result of an emergency.[44] The spending limits covered the five fiscal years following the SCA's enactment (1991-1996) and, subject to certain exceptions, could not be exceeded.[45] However, undoubtedly by design, the exceptions actually provided the legislature with

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[42] S.C. 1992, c. 19 [hereinafter *SCA*].

[43] R.S.C. 1985, c. 4-1.

[44] *Ibid.* at s. 2. The definitional section provided that "emergency" included an urgent and critical situation caused by drought, earthquake, fire, flood, storm, act of intimidation or coercion, threat to the security of Canada, real or imminent use of force or violence, war, armed conflict, accident or other occurrence that is so severe as to constitute a matter of serious national concern.

[45] *Ibid.* at s. 3(1).

considerable flexibility. For example, the SCA permitted overspending in any fiscal year provided that the government accounted for the excess spending in the following two fiscal years.[46] Furthermore, the statute expressly recognized the possibility of amending the spending limits for a particular fiscal year in order to ensure proper compliance with the Act.[47]

Ultimately, the government attempted to amend the spending limits, but not in the manner likely envisioned by the legislation's drafters. In fact, the spending limits established by the SCA were so high as to be rendered effectively meaningless. In order to further promote its fiscal rectitude, in 1993 the government proposed amending the SCA to provide for lower spending limits for the remainder of the five year period.[48] However, the SCA became a non-issue with the rise to power of the Liberal party and in 1994 Finance Minister Paul Martin chose not to extend the Act beyond its original five year period.[49]

The rising national debt throughout the 1990s provides, in retrospect, ample evidence of the negligible effect of the SCA.[50] In fact, the Standing Committee, which examined the Act prior to its enactment, was warned that this was likely to be the case but chose nevertheless to recommend the statute's adoption.[51] Although the SCA succeeded in increasing the level of disclosure with regard to budgetary matters,[52] its failure to rein in government spending demonstrates the perils of focusing exclusively on the spending side of government finance and the problems associated with using actual dollar figures rather than percentages relative to the overall economy in establishing deficit targets.

2. Spending Control Act[53] *(Alberta)*

Alberta followed the federal government's lead in 1992 by enacting a *Spending Control Act* of its own. That legislation, the first of three balanced budget statutes that the province enacted over a four year period, proved to be short-lived as it was repealed less than one year after its enactment.[54] Described as a unique and "important piece of legislation",[55] the government of the day claimed that the legislation complemented its

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[46] *Ibid.* at s. 3(3).

[47] *Ibid.* at s. 3(5).

[48] Bill C-130, *An Act to amend the Spending Control Act*, 3d Sess., 34th Parliament, 1991-93. The Progressive Conservatives lost power before enacting the bill.

[49] Canada, House of Commons, *Budget Plan Including Supplementary Information and Notices of Ways and Means Motions* (6 March 1996) at 135-7.

[50] *Fiscal Update, supra*, note 3.

[51] For example, Professor Douglas Hartle testified before the Standing Committee that the spending control program was little more than a public relations exercise given the loopholes the government had provided for itself. Canada, House of Commons, Standing Committee on Finance, "Consideration of the Proposed Spending Control Act", Issue No. 26 (26 November 1991) at 16.

[52] The Act also required the government to annually disclose its compliance with the Act. SCA, s. 6. Both the Conservative and Liberal governments adhered to this provision during the effective period of the Act.

[53] S.A. 1992, c. S-21.7.

[54] The Spending Control Act was repealed as a consequence of the enactment of the *Deficit Elimination Act.*

[55] *Alberta Hansard*, No. 84 (24 June 1992) at 1615.

"well understood fiscal policy... [of] moving towards a balanced budget".[56] However, closer examination of the legislation revealed that the opposition's characterization of the legislation as one that accomplished nothing, was more accurate.[57]

The statute required the government to limit increases in program spending, defined as all spending except for, among other things, debt servicing costs and guarantees and indemnities of the Crown,[58] to no more than 2.5 percent over a forecast base in the first year of the Act and declining to no more than 2.0 percent in the third year of the Act.[59] The Act, however, also established an important loophole that entitled the government to issue a special warrant authorizing expenditures not otherwise allocated.[60] Finally, the Act included an annual reporting requirement mandating a report disclosing compliance with the Act.[61]

The quick repeal of the Spending Control Act is indicative of its utility and impact on Alberta's fiscal policies. The loopholes in the Act enabled the government to authorize approximately $4.5 billion in expenditures above the prescribed limits[62] and the ease with which the Act was replaced provides further evidence of the non-binding nature of such legislation.

3. Expenditure Control Act[63] *(Nova Scotia)*

The third spending limitation statute, and the only one remaining in force, was enacted by Nova Scotia in 1993. Described by the government as "unprecedented" and by the opposition as a "toothless tiger",[64] the ECA was designed to reduce Nova Scotia's operating and capital expenditures over the four year period from 1994-5 through 1997-98.

The ECA defines operating expenditures as all current account expenditures, less gross debt and government restructuring charges.[65] The ECA establishes annual reductions of at least 2-3 percent in operating expenses and at least 5 percent in capital expenditures.[66] However, the ECA creates an exception to the spending reduction requirements if such spending is authorized by a resolution passed by the House of Assembly.[67] The ECA does not contain any penalty clauses should there be a failure to adhere to the spending cuts, nor are there any provisions mandating public disclosure of the government's performance in that regard.

Although the ECA creates a stricter framework than either of the Spending Control

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[56] *Ibid.*

[57] Mitchell, *supra* note 19.

[58] *Supra* note 52 at s. 1(d).

[59] *Ibid.* at s. 2.

[60] *Ibid.* at s. 4.

[61] *Ibid.* at s. 6.

[62] *Alberta Hansard*, No. 135 (10 May 1993) at 2656.

[63] *An Act Respecting the Reduction and Control of Operating and Capital Expenditures of the Province*, S.N.S.1993, c. 4 [hereinafter ECA].

[64] Nova Scotia, House of Assembly, *Debates and Proceedings* (18 November 1993) at 2694.

[65] Capital expenditures are defined as total capital expenditures. *Supra* note 61 at s. 3.

[66] *Ibid.* at ss. 5 & 6. Furthermore, s. 8 permits an exception to the capital expenditure provision by allowing for a decrease of only 4 percent in two of the Act's first three years.

[67] *Ibid.* s. 9.

Acts, its impact is also limited. The absence of a penalty provision may enable the government to evade the Act's provisions with little concern for the consequences. Moreover, the exceptions created for debt repayment in the operating expenditure definition and the omission of government revenues from consideration, resulted in skepticism over whether a balanced budget is likely to arise as a result of the ECA.

Aside from the increased publicity accorded to budgetary concerns, the Canadian experience with spending limitation legislation has little to commend it. Such legislation, at both the federal and provincial levels, has been plagued by gaping loopholes, a lack of accountability and the basic structural difficulty inherent in focusing solely on the spending side of the government's balance sheet.

B. *Balanced Budget Legislation*

1. Taxpayer Protection Act[68] *(British Columbia)*

Only months prior to its electoral defeat in 1991, the B.C. Social Credit government enacted the TPA. The legislation had two main goals: a three year tax rate freeze and a commitment to balance the provincial budget over a five year period.[69] Enacted with incredible hyperbole the legislation was, described by then-Premier Vander Zalm as "the greatest achievement by any government in this province's history or this country's history".[70]

Although somewhat skeptical at the time, the opposition New Democratic Party voted unanimously for the TPA.[71] The NDP action highlights the quandary opposition parties often find themselves in when confronted with balanced budget legislation. While they may regard the legislation as little more than an opportunistic political document, voting against balanced budgets is akin to voting against family and hockey. Therefore, faced with no viable alternative, opposition parties often make their criticisms known but ultimately support the actions of the government. In this instance, however, the NDP was able to quickly reverse itself. The NDP replaced the Social Credit party as the government in power only months after passage of the TPA. In one of their first acts as the governing party, they enacted the *Taxpayer Protection Repeal Act*,[72] which effectively nullified any effect the TPA may have had.

Notwithstanding its quick demise, the TPA provided an early indication of some of the issues to be dealt with when enacting balanced budget legislation. Under the Act, the government was required to present an annual "Balanced Budget Plan". The plan was to contain balanced revenue and expenditure forecasts for the following five fiscal years.[73] Furthermore, the legislation provided that increases in forecast expenditures for the first year of each plan could not exceed the preceding year's expenditures by more than the average, previous five-year provincial GDP growth.[74] Finally, the TPA required

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[68] S.B.C. 1991, c. 6.

[69] Although beyond the scope of this article, it should be noted that the taxation component of the legislation instituted a three year tax freeze on some, but not all, provincial taxes.

[70] *Supra* note 18.

[71] British Columbia, *Debates of the Legislative Assembly*, No. 2 (15 April 1992) at 794.

[72] S.B.C. 1992, c. 23.

[73] *Ibid.* at ss. 8, 9, & 10.

[74] *Ibid.* at s. 11.

the government to table both an annual Balanced Budget Progress Report highlighting the previous year's performance and the cumulative performance since 1991,[75] and a Debt Reduction Plan report aimed at reducing the public debt.[76]

Opponents of the legislation seized upon the shortcomings of the TPA, which provided the NDP with a built-in rationale for the Act's subsequent repeal. For instance, the TPA contained no penalty provisions and thus no means of ensuring compliance. Furthermore, the Act provided no detail as to how to balance the budget; it merely required that each five year plan balance. Most problematic, however, was the fact that new five year plans were to be presented annually. Therefore, the government could present a balanced five year plan in Year One with deficit spending that year and in Year Two simply roll in the increased debt resulting from the deficit spending by presenting a new balancing five year plan. In effect, the government could run deficits on a rolling basis by merely projecting a balanced budget sometime in the future, although this would admittedly become increasingly difficult to do. The TPA, though short-lived, never really provided a viable means of achieving a balanced budget. Rather, it provides an example of pre-election posturing and demonstrates the ease of amending or repealing such legislation as well as the difficulty inherent in devising legislation that genuinely compels a government to balance its budget.

2. Deficit Elimination Act[77] *(Alberta)*

The popularity of balanced budget legislation began to rise in earnest in Canada in 1993, when following the economic recession of the early 1990s, governments increasingly turned their attention to "serious" methods of deficit reduction. Alberta led the way in this regard, passing the DEA less than one year after its enactment of the Spending Control Act. The government hailed the DEA as "precedent-setting" and a "landmark piece of legislation".[78] Not surprisingly, with an election in the offing, the opposition remained skeptical, noting the quick repeal of the Spending Control Act and labelling the legislation "nothing more than...an example of public relations".[79] Notwithstanding their skepticism, the DEA was, in fact, the most comprehensive Canadian balanced budget statute at that time. It succeeded in remedying several of its predecessors' shortcomings by providing for increased disclosure and flexibility, and by establishing a balanced and realistic approach to deficit reduction.

The Act sought to achieve its goal of deficit elimination in four years by establishing annual maximum deficit targets. These ranged from a high of $2.5 billion in the 1993-94 fiscal year descending to $0 in 1996-97.[80] Unlike the previously examined statutes, the DEA defined the deficit as the difference between government revenue and expenditures, if expenditures exceed revenues.[81] Expenditures were defined as all Crown expenditures for all purposes; no exceptions were made for debt payments

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[75] *Ibid.* at s. 13.
[76] *Ibid.* at s. 12.
[77] S.A. 1993, c. D-6.5 [hereinafter DEA].
[78] *Alberta Hansard*, No. 142 (14 May 1993) at 2788.
[79] *Alberta Hansard*, No. 135 (10 May 1993) at 2653.
[80] *Supra* note 75 at s. 2.
[81] *Ibid.* at s. 1(b).

or other liabilities.[82]

Although the Act included no penalty provisions, it contemplated the possibility of missing the deficit targets. In particular, the DEA provided that if the actual deficit exceeded the mandated target, the subsequent year's deficit target would be reduced by a corresponding amount.[83] Accordingly, the statute ensured that the government could not roll over the increased debt as might have occurred under B.C.'s TPA. However, if the actual deficit were lower than the target deficit, the statute prohibited increasing the subsequent year's deficit by a corresponding sum.[84]

The Act also sought to increase disclosure and inject greater "realism" into the budgetary process. For example, the Act required the government to adopt particularly conservative estimates for its projected revenues.[85] Moreover, special warrants to authorize unanticipated expenditures were permitted only in the event of the dissolution of the Legislative Assembly or of an "emergency or disaster".[86] Finally, the Act mandated significant reporting requirements including an annual report from the province's Audit Committee and quarterly reports from the Provincial Treasurer.[87]

Although the Act adopted a conservative and strict approach to deficit reduction, its most significant defect was the absence of a penalty provision. An attempt to remedy this was made several months after the enactment of the DEA as the opposition introduced the *Deficit Elimination Amendment Act, 1993*.[88] The DEAA provided for the introduction of strict penalties for failure to meet the Act's deficit targets referred to. In particular, failure to meet the targets in the first year would have resulted in a 5 percent reduction in all MLA salaries. Furthermore, failure to meet the second year targets would have compelled the government to resign and call a general election.[89]

Although derided as "theatrics"[90] and defeated at second reading,[91] the DEAA highlighted a significant shortcoming in many balanced budget statutes, namely the absence of an effective enforcement mechanism to better ensure compliance with the legislation in question. Notwithstanding the Alberta government's reluctance to adopt penalty provisions such as those proposed in the DEAA, the proposal foreshadowed the ongoing debate regarding balanced budget legislation and may have served as a model for Manitoba's balanced budget statute, discussed further below.

3. An Act Respecting the Balancing of the Ordinary Expenditures and Ordinary Revenues of the Province [92]*(New Brunswick)*

New Brunswick joined the trend toward balanced budget legislation with a statute of its own in the spring of 1993. Unlike other balanced budget statutes the NBBBL

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[82] *Ibid.* at s. 1(c).

[83] *Ibid.* at s. 3.

[84] *Ibid.* at s. 4.

[85] *Ibid.* at s. 5(1).

[86] "Emergency or a disaster" however, as is defined by the legislation. *Ibid.* at s. 6.

[87] *Ibid.* at ss. 8 & 9.

[88] Bill 202, *Deficit Elimination Amendment Act, 1993*, 1 [st]sess., 23rd Leg. Alberta [hereinafter DEAA].

[89] *Alberta Hansard*, No. 33 (2 September 1993) at 35.

[90] *Alberta Hansard*, No. 14 (15 September 1993) at 269.

[91] *Ibid.* at 278.

[92] S.N.B. 1993, c. B-0.1 [hereinafter NBBBL].

made little attempt to pretend to be anything other than an objective of the government.[93] This was clearly expressed in Section 2 of the NBBBL which stated that "[i]t is the *objective* of the Government of New Brunswick that the total amount of the ordinary expenditures for a fiscal period not exceed the total amount of the ordinary revenues for that fiscal period" [emphasis added].[94] The fiscal period referred to was for a three year period from 1993 to 1996.[95]

The balancing requirements mandated by the Act were less stringent than those found in comparable legislation. For example, the Act specified that the determination of a balanced budget would not take a change in federal transfer payments into account.[96] Therefore, not only did the NBBBL not require a balanced budget, but it also established important exceptions to the very definition of a balanced budget.

Notwithstanding the statute's significant shortcomings, the NBBBL succeeded in two respects. First, the Act increased the degree of clarity and disclosure in the budgetary process by mandating annual progress reports[97] and prohibiting the use of altered accounting practices to enhance the previous year's fiscal performance.[98] Second, the Act recognized the need for flexibility in achieving a balanced budget by setting such an objective over a three year fiscal period rather than on an annual basis, thereby allowing for downward swings in the economy.

4. Balanced Budget and Debt Retirement Act [99] *(Alberta)*

The watershed year for balanced budget legislation in Canada was 1995 with four Western provinces and territories, Alberta, the Northwest Territories, Saskatchewan, and Manitoba, all enacting or amending balanced budget legislation. The first to do so was Alberta, as it enacted the BBDRA as a progression of its earlier balanced budget legislation activities. Unlike the DEA, which resulted in the repeal of Alberta's Spending Control Act, the BBDRA is designed to complement and, in fact, enhance the earlier statute. The BBDRA, lauded as the "first of its kind",[100] has since garnered significant praise from analysts.[101]

Although much of the BBDRA is devoted to the development of a debt repayment plan, the Act also touches on issues pertaining to the provincial deficit. In particular, the Act reaffirms the goal of balanced budgets by explicitly providing that "[e]xpenditures during a fiscal year must not be more than revenue".[102] Moreover, the

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[93] It should be noted, however, that this was not always the case. When the legislation was first introduced to the provincial legislature, the government spoke in terms of "requiring" a balanced budget. *Journals of the House of Assembly of the Province of New Brunswick* (8 December 1992) at 4876.

[94] *Supra* note 90 at s. 2.

[95] The NBBBL contemplated extension of the Act as it provided for an indefinite number of "subsequent fiscal periods" of four years each. *Ibid.* at s. 1.

[96] *Ibid.* at s. 6.

[97] *Ibid.* at s. 3.

[98] *Ibid.* at s. 5.

[99] S.A. 1995, c. B-0.5 [hereinafter BBDRA].

[100] *Alberta Hansard*, No. 24 (13 March 1995) at 514.

[101] See, *e.g.*, "Alberta and its Deficit", *The Globe and Mail* (26 June 1996) A14.

[102] BBDRA, s. 2. Note that "expenditures" and "revenue" are defined as all expenditures and revenue of the government, without exception. *Ibid.* at s. 1.

Act mandates that any surplus revenue generated during a fiscal year be applied to reducing the Crown debt and not used to increase spending.[103] Finally, the Act also establishes increased reporting requirements. In addition to the quarterly reports mandated by the DEA, as a result of the BBDRA all budgetary reports must also advise on the progress made toward retirement of the provincial debt.[104]

The BBDRA provides some indication of how legislation may look once a budgetary deficit has been eliminated or reduced to "reasonable" levels. However, although it may be an impressive achievement to reduce or eliminate a provincial deficit,[105] the wisdom of legislating debt repayment is open to question.[106] Like the DEA before it, the BBDRA contains no penalty provisions and no means of assuring compliance. A recent editorial seized upon this deficiency as the columnists noted that although the Alberta government had pledged to use any surplus income to pay down the debt, it could easily target the income for other purposes since "...rules are made to be broken, and there is absolutely nothing...stopping the Klein government from passing a new law".[107]

5. Deficit Elimination Act[108] *(Northwest Territories)*

With little fanfare, the Northwest Territories enacted its own balanced budget legislation in 1995. Interestingly, although the legislation mandates a balanced budget by the 1997-98 fiscal year, the government has made scant mention of its *legal* requirement to reduce its deficit in its statements regarding the fiscal health of the territory. For example, in 1995 and 1996 sessional statements by Premier Don Morin, the need to balance the budget was commented on repeatedly, without mention of the NWDEA.[109] Similarly, the budget addresses for both the 1996-97 and 1997-98 fiscal years discuss at length the efforts to balance the budget, yet do not mention the NWDEA.[110]

The NWDEA takes a fairly straightforward approach to deficit reduction. The Act sets fiscal targets for three fiscal years with the deficit capped at $45 million dollars in the first year, two percent of revenues in the second year, and a balanced budget in the third year.[111] The NWDEA defines deficit as the difference between revenue and

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[103] *Ibid.* at s. 6.

[104] *Ibid.* at ss. 7(1), 7(2).

[105] Though, as noted above, this too is subject to debate.

[106] Although beyond the scope of this article, the rise in popularity of debt repayment legislation raises several issues of concern. In particular, while the logic behind deficit reduction can be readily appreciated, one wonders whether zero debt is a similarly appropriate goal. Further, the extent to which debt repayment should be legislatively tied to a prescribed schedule rather than rise and fall in accordance with general economic performance has not been conclusively addressed.

[107] K. McKenzie and R. Kneebone, "The Logic — and the Law — of the Klein Debt-Decision" *The [Vancouver] Sun* (26 June 1996) A13.

[108] S.N.W.T. 1995, c. 22 [hereinafter NWDEA].

[109] *Northwest Territories Hansard* (13 December 1995) at 27; *Northwest Territories Hansard* (27 November 1996) at 2.

[110] *Supra* note 105 at s. 2.

[111] *Ibid.* at s. 2.

expenditures if expenditures exceed revenue.[112] The definitions of both expenditures and revenues comprehensively cover all cash flows.[113]

In the event that the deficit targets are not met, the NWDEA provides two courses of action. First, the Act adjusts the subsequent year's deficit target (or requires a surplus in the case of the final year) to ensure that the three year projections are still achieved.[114] Second, the Act establishes a very ineffectual penalty provision.[115] In particular, in the event of a deemed contravention of the Act,[116] the Legislative Assembly is required to consider whether the Cabinet should resign. Although a forced Cabinet resignation would clearly be a very powerful penalty provision, given that the governing party controls the Legislative Assembly, use of this provision seems very unlikely. Furthermore, the disclosure requirements are unimpressive since they require only that unconsolidated public accounts be tabled before the Legislative Assembly as soon as reasonably practicable.[117]

Although the NWDEA provides for strict deficit targets, its supplementary provisions, such as penalty provisions and disclosure requirements are somewhat disappointing. However, given the success of the government in achieving its goals[118] and the lack of attention paid to the Act following its enactment, perhaps the lesson best learned from the Northwest Territories' experience is that deficit cutting does not require legislation; it requires political will and leadership.

6. The Balanced Budget Act [119] *(Saskatchewan)*

Close examination of the BBA, Saskatchewan's version of a balanced budget statute enacted in the spring of 1995, reveals that its drafters put a premium on flexibility. Although decried by the opposition as a "political ploy",[120] the government seemed to recognize that previous balanced budget legislative failures owed much to an excessive degree of restrictiveness that left politicians with few options other than to amend, repeal or violate the statute in question.[121]

The BBA requires each newly elected government to prepare a four-year financial plan and a debt management plan.[122] The four-year financial plan must balance over the fiscal four year period rather than each fiscal year[123] and, unlike B.C.'s TPA, is not subject to revision each year. Rather, the plan provides a barometer with which the public is able to gauge the government's success in balancing the books. Ostensibly designed to mirror an economic cycle, it should be noted that the legislation in fact

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[112] *Ibid.* at s. 1.

[113] *Ibid.*

[114] *Ibid.* at s. 3.

[115] *Ibid.* at ss. 5(2)(3).

[116] A "deemed contravention" occurs where the deficit targets prescribed by the Act are not achieved. *Ibid.* at s. 5(2).

[117] *Ibid.* at s. 4(2).

[118] "N.W.T. To Eliminate Deficit" *The [Vancouver] Sun* (28 January 1997) A3.

[119] *An Act to Maintain Financial Stability and Integrity in the Administration of the Finances of the Province of Saskatchewan*, S.S. 1995, c. B-0.01 [hereinafter BBA].

[120] Saskatchewan, Legislative Assembly, *Debates and Proceedings* (18 May 1995) at 2480.

[121] *Ibid.* at 2481.

[122] *Supra* note 116 at s. 3.

[123] *Ibid.* at s. 4(1).

follows the *electoral* cycle. Therefore, although the four year period provides the government with a more flexible time frame for action, it does not alleviate the economic concerns regarding fiscal adjustments during economic slowdowns.

The Act provides further flexibility by permitting funds to be exempted from the balancing requirement in the event that "a major, unanticipated, identifiable event or set of circumstances has had a dramatic impact on expenses or revenues in a fiscal year".[124] Although critics note that this provision severely curtails the "mandatory" nature of the Act, it could equally be interpreted as taking a more realistic approach to balanced budget legislation.[125]

The BBA also contains a series of precautionary provisions. These include stipulations that income generated by sales of Crown corporations not be used to increase expenditures,[126] that changes to accounting policies be duly noted and not used to determine if the balancing requirement has been met,[127] and that the government prepare an annual report disclosing the status of the economy with regard to achieving a balanced budget and containing a revised forecast of revenues and expenditures.[128] The BBA does not contain a penalty provision for violation of the Act, leaving the legislation with considerable flexibility but without an effective enforcement mechanism.

7. The Balanced Budget, Debt Repayment and Taxpayer Protection and Consequential Amendments Act [129] *(Manitoba)*

Manitoba enacted the fourth and final balanced budget statute of 1995 following months of debate within the province. The government introduced the statute in March 1995, just prior to the provincial election but without sufficient time for passage.[130] Once re-elected, the Filmon government re-introduced the legislation in June of that year and ultimately passed it into law in November. The debate surrounding the BBTPA was particularly vociferous, in large measure due to the breadth of the statute. Specifically, the BBTPA establishes a balanced budget requirement, a debt repayment schedule, and a referendum requirement prior to the implementation of any future tax rate increases on several taxes.

The balanced budget provisions contained in the Act are among the most comprehensive to be enacted in Canada. The BBTPA mandates that the province's budget balance each fiscal year rather than over a longer period as in Saskatchewan's BBA.[131] To cushion the impact of this strict provision, the Act establishes several exceptions to the general rule. The exceptions provide that the Act is deemed not violated, notwithstanding a failure to balance the budget, in the event that an expenditure is required as a result of a natural or other disaster in Manitoba that could

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[124] *Ibid.* at s. 4(2).

[125] In the event that such a set of circumstances transpires, the Act requires the government to present a special report identifying the events or circumstances and the financial implications of the events or circumstances. Note, however, that the Act does not define these terms. *Ibid.*

[126] *Ibid.* at s. 9(2).

[127] *Ibid.* at s. 4(3).

[128] *Ibid.* at ss. 6 & 8.

[129] S.M.1995, c. 7[hereinafter BBTPA].

[130] *Manitoba Hansard* (15 March 1995) at 951.

[131] *Supra* note 126 at s. 2.

not have been anticipated and affects the province in a manner that is of urgent public concern; required because Canada is at war or under apprehension of war; or required as a result of a reduction in revenue of five percent or more, other than a reduction resulting from a change in Manitoba's taxation laws.[132]

The specificity of these exceptions is necessary in light of the penalty provisions contained in the Act. In particular, the BBTPA mandates that in the event of a deficit in a particular year, the government must achieve at least an offsetting surplus in the next fiscal year.[133] Furthermore, the Act establishes fiscal penalties should such a failure to comply with the Act transpire. Pursuant to section 7(1) of the Act, members of the Executive Council of the government face a 20 percent reduction in pay for a one-year non-compliance with the Act and a 40 percent reduction in pay for failure to comply in consecutive years.[134] These penalty provisions are unique in Canada and, though subject to criticism,[135] provide the BBTPA with the strongest enforcement mechanism currently in force.

Applauded by some analysts as the centrepiece of an "economic revolution",[136] the BBTPA meets many of the criteria discussed below as necessary for an effective balanced budget statute. In particular, the inclusion of penalty clauses, the requirement to balance expenditures with revenues and the flexibility created by the exceptions to the balanced budget requirement provide Manitoba with Canada's best hope for an effective balanced budget statute. However, the legislation is not infallible as it does not significantly increase public disclosure of the budgetary process[137] and its adherence to an annual balancing may leave some concerned about the impact of a long-term economic downturn.[138]

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[132] *Ibid.* at s. 3(2).

[133] *Ibid.* at s. 4.

[134] *Ibid.* at s. 7.

[135] MLA Wowchuk argued that "I think we could see the ministers actually punishing the poor and cutting programs in order to keep their budget in line just so they would not lose their salaries." Although that might not be the most politically astute course of action, Wowchuk's point of the potential for conflict of interest is a good one. *Manitoba Hansard* (4 October 1995) at 3652.

[136] See, *e.g.*, L. Gunter, "Manitoba Tories Pull Off Major Economic Revolution" *The [Edmonton] Journal* (9 November 1995) A18; R. Richardson, "Manitoba Leads on Balanced Budgets" *The Financial Post* (31 August 1995) 9.

[137] Section 5 of the Act provides only for the release of audited financial statements to be released within six months of the completion of a fiscal year. Moreover, s. 6 of the Act mandates reports on compliance with the Act in the third quarter of the fiscal year.

[138] A proposed amendment to the BBTPA, which would have created an exception to the balanced budget requirement in the event that:

> "Manitoba's economy is in recession at any time in the fiscal year and, for this purpose, the economy shall be considered to be in a recession at a time if Manitoba's gross domestic product has declined for the last two consecutive quarters ending before that time;"

was defeated by a voice vote in the Legislative Assembly. *Manitoba Hansard* (27 October 1995) at 4318-9.

8. An Act Respecting the Elimination of the Deficit and a Balanced Budget [139] *(Quebec)*

In response to widespread pressure to address its economic woes,[140] Quebec became the latest province to undertake steps toward the adoption of balanced budget legislation in May 1996. Although Finance Minister Bernard Landry has described the Quebec Bill as Canada's toughest anti-deficit law,[141] close examination of the text reveals that Landry's claims are somewhat exaggerated.[142]

The Quebec Act bears a strong resemblance to Alberta's DEA, establishing maximum annual deficit targets beginning in 1996-97 at $3.275 billion and declining by approximately $1 billion per year to a balanced budget by 1999-2000.[143] The Act also mandates that no further deficits be incurred thereafter.[144] The Quebec Act does, however, establish several exceptions to these deficit requirements. For example, the legislation provides that the government may exceed the deficit targets by up to $1 billion per year provided that the shortfall is made up the following fiscal year.[145] In addition, the government may exceed the deficit targets by over $1 billion per year in the event that there has been a disaster[146] which has had a major impact on revenues or expenditures; there has been a significant deterioration of economic conditions; or there has been a change in federal transfer payments substantially reducing transfer payments to the Quebec government.[147] However, should one of these events occur, the government must offset the shortfall over the following five fiscal years.[148]

Although the Quebec Act establishes fairly strict deficit cutting targets, the proposed legislation falls short in several respects. First, the Act has no penalty provisions to ensure compliance. Second, the Act does not provide for increased disclosure with regard to budgetary issues.

IV. FOREIGN EXPERIENCE WITH BALANCED BUDGET INITIATIVES

Although a comprehensive comparative analysis is beyond the scope of this article, an examination of several other jurisdictions experiences with balanced budget legislation provides some interesting insights into the effectiveness of various types of provisions. In particular, the experiences of the United States at the both the federal and

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[139] Bill 3, *An Act Respecting the Elimination of the Deficit and a Balanced Budget*, 2d Sess., 35th Leg. Quebec,1996 [hereinafter Quebec Act]. Now S.Q. 1996, c. 55 came into force December 23, 1996.

[140] Scowen, *supra* note 7.

[141] S. Scott, "Law to Require Balanced Budget by 2000: But Loophole Allows Extension for Recession, Cut in Transfer Payments" *The [Montreal] Gazette* (10 May 1996) A8.

[142] D. MacPherson, "Anti-Deficit Law a Sham: Allows $1 Billion 'Margin of Error'" *[Montreal] Gazette* (16 October 1996) B3.

[143] Quebec Act, ss. 3 - 6.

[144] Quebec Act, s. 6.

[145] Quebec Act, s. 8. It is interesting to note that if a surplus is achieved in a fiscal year, the government may exceed subsequent deficit targets by an equivalent amount. Quebec Act, s. 9.

[146] The Act does not define "disaster".

[147] Quebec Act, s. 10.

[148] Quebec Act, s. 11.

state levels, the European Union, and New Zealand are instructive. These jurisdictions, all having enacted some form of balanced budget legislation, have witnessed first hand the effectiveness of genuine penalty provisions, the problems arising from insufficient flexibility, and the advantages of increasing the level of public disclosure.[149]

As noted in Part I, however, there are fundamental differences in budgetary processes between Canada and these other jurisdictions, particularly the United States.[150] For example, unlike the U.S. practice of mandating budgetary approval from both the executive and legislative branches of government, the Canadian budgetary process relies primarily upon the power of the Prime Minister/Premier and the Finance Minister/Provincial Treasurer.[151] Therefore, though foreign experiences provide helpful insights, some of the specific experience and analysis is inapplicable in a Canadian context.

A. *United States*

In many respects, the U.S. and Canadian experiences with rising national debts and consecutive budget deficits are strikingly similar.[152] For much of its history, the U.S. rarely ran a budget deficit.[153] Following World War II deficit financing became increasingly commonplace.[154] As in Canada, the U.S. federal debt began to spiral out of control in the late 1970s. In the 12 years of the Reagan and Bush presidencies, the accumulated U.S. national debt rose from nearly $1 trillion to approximately $3.5 trillion.[155] Not surprisingly, U.S. politicians responded to the perceived budgetary crises with a series of attempts to enact balanced budget legislation.

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[149] Although the comparative analysis conducted herein is limited to the three jurisdictions discussed, they are not the only jurisdictions to experiment with some form of balanced budget legislation. For example, Article 110 (1) of Germany's *Constitution* provides that "[t]he budget has to be balanced as regards revenue and expenditure." However, Article 115 allows for some flexibility in this regard as it provides that a balanced budget is defined as one where expenditures do not exceed the sum of revenues plus net borrowing for investment purposes. Moreover, Germany has also enacted legislation that grants the government greater discretion in running budgetary deficits. U.S. General Accounting Office (GAO), *Deficit Reduction: Experiences of Other Nations* (Washington: GAO/AIMD-95-30, December 1994) at 129-30.

Similarly, Japan's *Public Finance Law of 1947*, the basic budget law in Japan, originally permitted the government to issue bonds only if the funds were to be used for public works, investment, and governmental loans. This law was amended in 1975, however, to permit special deficit financing bonds. *Ibid.* at 150-1.

[150] For an interesting review of the Canadian budgetary process, see, A.M. Maslove, M.J. Prince, & G.B. Doern, *Federal and Provincial Budgeting* (Toronto: University of Toronto Press, 1986).

[151] *Ibid.*

[152] Notwithstanding the similar deficit history, the differing governing and budgetary approaches should be borne in mind when contrasting the two countries' experiences. For further details on the U.S. budgetary process, see, A. Wildavsky, *The New Politics of the Budgetary Process* (Berkeley: Harper Collins Publishers, 1988).

[153] Advisory Commission on Intergovernmental Relations (ACIR), *Fiscal Discipline In The Federal System: National Reform And The Experience Of The States* (Washington: 1987) at 3.

[154] *Ibid.*

[155] N. Devins, "Budget Reform and the Balance of Powers" (1990) 31 William and Mary L. Rev. 993 at 993.

One of the first such attempts was the enactment of the *Congressional Budgeting and Impoundment Control Act of 1974*.[156] Under the 1974 Budget Act, the U.S. Congress established spending targets on certain programs. The measure failed to adequately control government spending since the spending targets became mere aggregate spending totals rather than genuine constraints.[157] Moreover, by focusing exclusively on the spending side of the deficit equation, the 1974 Budget Act failed to account for revenues, enabling the deficit to rise in spite of the spending caps.[158]

The next Congressional attempt to enact some form of balanced budget legislation came in 1978 in the form of a little known section in the *Bretton Woods Agreement Act*.[159] Section 7 of the BWAA provided that "[b]eginning with fiscal year 1981, the total budget outlays of the Federal Government shall not exceed its receipts".[160] Notwithstanding the existence of this provision, however the budgetary process in the early 1980s largely ignored the BWAA.

The rising deficit and national debt of the early 1980s resulted in an increased urgency to undertake legislative action. While many advocated a constitutional balanced budget amendment,[161] universal agreement on the necessary scope and wording of such an amendment proved unattainable. As an alternative, a statutory solution was sought. First, Congress passed the *Spending Reduction Act of 1984*,[162] legislation that, like the BWAA, was largely ignored.

Following the failed 1984 legislation, Congress passed The Balanced Budget and Emergency Deficit Control Act of 1985, popularly known as the Gramm-Rudman-Hollings Act.[163] Hailed by then President Reagan as an important step toward putting the U.S. fiscal house in order, GRH 1985 received wide support in both houses of Congress.[164] GRH 1985 was perceived to be an effective new approach to balancing the budget because it sought to impose legal and institutional constraints against deficit growth. For example, it mandated that if the President and Congress were unable to agree on a deficit-reducing budget that achieved the targets specified in the legislation, then it would impose automatic spending cuts, referred to in the legislation as "sequestration".[165] The automatic spending cuts were to be imposed equally to all spending programs that were subject to GRH 1985. Accordingly, the imposition of

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[156] 2 U.S.C. Sec. 601-688 (1982) [hereinafter 1974 Budget Act].

[157] E. D. Elliott, "Regulating the Deficit After *Bowshar* v. *Synar*" (1987) 4 Yale J. on Reg. 317 at 356.

[158] *Ibid.*

[159] *Bretton Woods Amendment Act*, Pub. L. No. 95-435, 92 Stat. 1051 1978 (codified as amended in scattered sections of 22 & 31 U.S.C.) [hereinafter BWAA].

[160] *Ibid.*

[161] See, *e.g.*, A. Wildavsky, *How To Limit Government Spending* (Berkeley: University of California Press, 1980). For an excellent historical review, see D.E. Kyvig, "Refining or Resisting Modern Government? The Balanced Budget Amendment to the U.S. Constitution" (1995) 28:2 Akron L. Rev. 97.

[162] *Spending Reduction Act of 1984*, Pub. L. No. 98-369, ss. 2161-2103, 98 Stat. 494, 1057-8.

[163] *Balanced Budget and Emergency Deficit Control Act of 1985*, Pub. L. No. 99-177, 99 Stat. 1038 (codified as amended in scattered sections of 2, 31, & 42 U.S.C.)[hereinafter GRH 1985].

[164] K. Stith, "Rewriting the Fiscal Constitution: The Case of Gramm-Rudman-Hollings" (1988) 76 Cal. L. Rev. 593 at 596.

[165] *Ibid.* at 597.

sequestration was, in effect, a penalty provision designed to create a sufficiently unattractive threat to ensure the attainment of a deficit-reducing budgetary agreement.[166]

It soon became apparent, however, that GRH 1985 was not as effective as initially envisioned. First, the legislation established maximum amounts that could be sequestered rather than permitting sequestration of all funds above the deficit targets. For example, for the fiscal year 1986, the maximum sequestration was set at $11.7 billion while the actual deficit exceeded the GRH 1985 maximum by $172 billion.[167] Although the sequestration process worked as planned, it failed to acheive the maximum deficit targets were achieved. Second, numerous spending programs were not subject to GRH 1985 sequestration. These programs, often referred to as the "uncontrollable" portion of the budget, included most annually appropriated and all permanently appropriated programs, including social security entitlement, and prior legal obligations.[168] Third, the GRH 1985 imposed maximum deficit targets applied only to deficits projected in the budget, not to actual deficits. By employing exaggerated figures for expenditures and revenues, compliance with GRH 1985 was possible without any genuine hope of actually fulfilling the projections at the end of the fiscal year.[169]

The U.S. Supreme Court dealt a further blow to GRH 1985 when it ruled in *Bowsher v. Synar*[170] that a key provision in the legislation was unconstitutional. Although acknowledging that GRH 1985 was enacted "to meet a national fiscal emergency...of unprecedented magnitude",[171] the court ruled that placing responsibility for execution of the legislation into the hands of an officer removable only by Congress violated the Constitution by intruding onto the executive function.[172] In response, in 1987 Congress amended GRH 1985 by delegating the sequestration responsibility to the Office of Management and Budget (OMB) in the Executive Office of the President.[173]

Notwithstanding its prior failures, Congress tried again in 1990 to enact balanced budget legislation by replacing GRH 1985 with the *Budget Enforcement Act of 1990*[174]. The BEA shifted the focus away from deficit control and back to expenditures. Specifically, the BEA stipulated maximum limits on discretionary spending.

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[166] *Ibid.* at 624.

Thomas Schelling refers to the imposition of such penalty clauses as "enforcing rules on oneself." Schelling notes that enforcement rules must make a violation unattractive through the attachment of credible penalties and simultaneously keep a violation from causing the whole enterprise to collapse. T. Schelling, "Enforcing Rules on Oneself" (1985) 1 J.L. Econ. & Org. 357. See also, P.W. Kahn, "Gramm-Rudman and the Capacity of Congress to Control the Future" (1986) 13 Hastings Const.. L. Q. 185.

[167] *Supra* note 14 at 630.

[168] *Ibid.* at 631.

[169] Wrobel, *supra* note 8 at 9.

[170] *Bowsher v. Synar*, 106 S. Ct. 3181 (1986) [hereinafter *Bowsher*]. For further details on this case, see, E. Richards, "The Gutting of Gramm-Rudman: Implications for Bureaucrats, Budgets, and the Balance of Power" (1987) 22 N.E. L. Rev. 1.

[171] Bowsher, *ibid.* at 3192-3.

[172] The provision at issue directed the Comptroller General to prepare a report to the President and Congress specifying the program-by-program reductions necessary to prevent the prescribed maximum deficit level from being exceeded.

[173] *Balanced Budget and Emergency Deficit Control Reaffirmation Act of 1987*, Pub. L. No. 100-119, 101 Stat. 754.

[174] *Budget Enforcement Act of 1990*, Pub. L. No. 101-508, 104 Stat. 1388-573 [hereinafter BEA].

Furthermore, the BEA established a sequestration process similar to the one found in the amended GRH 1985. However, by exempting entitlement programs, which constituted an ever-increasing portion of the budget, and failing to establish an effective penalty provision, BEA's failure was almost guaranteed.

Although some analysts have continued to advocate the adoption of balanced budget legislation or a balanced budget constitutional amendment,[175] it should be noted that the U.S. deficit has, in fact, decreased in recent years. For example, according to the Congressional Budget Office the deficit for the 1996 fiscal year will be approximately $145 billion. Although a staggering sum, particularly by Canadian standards, that figure is actually half of the total recorded deficit in 1992. Moreover, the U.S. debt-to-GDP ratio has decreased from 4.9 percent in 1992 to 1.9 percent in 1996.[176] Furthermore, in January 1997 the President was provided with the power of a line item veto.[177] Long regarded as an effective means of eliminating wasteful spending or "pork", the veto enables the President to remove specific, appropriated expenditures without simultaneously rejecting the entire spending package, as would have occurred previously.[178]

The experience at the U.S. state level is also instructive. At present, 49 of the 50 U.S. states (all except Vermont) have some form of balanced budget requirement.[179] These approaches include a line item veto that grants a state governor the power to eliminate or reduce items in an appropriation;[180] the use of multiple budget bills to decrease the number of "objectionable" appropriations;[181] a requirement that all funds be appropriated thereby eliminating permanent entitlements;[182] a constitutional balanced budget requirement;[183] or a tax and expenditure limitation (TEL), that, as the name suggests, places limitations on increasing state taxes and expenditures.[184]

In view of their similarity to the Canadian experience, the constitutional balanced budget requirement and the TELs are of the greatest interest. Contrary to their proponents' expectations most empirical research has found that both of these

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[175] For example, a recent attempt to win passage of a constitutional balanced budget amendment in the Senate failed by only one vote. "Politics This Week" *The Economist* (8 March 1997) 6.

[176] J. Cassidy, "Ace in the Hole" 72 (15) New Yorker (10 June 1996) 36 at 37.

[177] *Line Item Veto Act*, Pub. L. No. 104-130, 110 Stat. 1200 (1996).

[178] For a good assessment of the merits of the line item veto, see M.L. Stearns, "The Public Choice Case Against the Item Veto" (1992) 49 Wash. & Lee L. Rev. 385.

[179] D.A. Kenyon & K.M. Benker, "Fiscal Discipline: Lessons from the State Experience" 37 Nat. Tax J. 433.

[180] For further detail on the state experience with line item vetoes, see Devins, *supra* note 152.

[181] Some argue that the greater the number of budget bills, the fewer the number of "objectionable" appropriations. This results from the fact that with fewer budget bills, legislators are more likely to accept objectionable appropriations for the overall good of approving the budget. W.M. Crain & J.C. Miller III, "Budget Process and Spending Growth" (1990) 31 William & Mary L. Rev. 1021 at 1025-7.

[182] This requirement endeavours to minimize or eliminate the "uncontrollable" portion of the budget, such as permanent entitlements. At least 21 states require that all funds to be appropriated periodically. *Ibid.* at 1028.

[183] 25 states have a constitutional balanced budget requirement. *Ibid.* at 1029.

[184] 19 states have adopted a TEL. D.G. Bails, "The Effectiveness of Tax-Expenditure Limitations: A Re-evaluation" (1990) 49 Am. J. of Econ. & Soc. 223 at 223.

approaches have had limited or no effect on government spending or deficit reduction.[185]

In the case of the constitutional balanced budget requirement, analysts have discovered a proclivity among state legislators to circumvent the requirement by issuing non-guaranteed debt, issuing debt through state agencies or obtaining supermajority approvals to override the requirement.[186] Although such action is often undertaken to facilitate capital financing as opposed to current expenditures, from a Canadian perspective such a distinction is immaterial since the issue of deficit financing encompasses both current and capital expenditures, insofar as these expenditures impact annual deficit targets. Therefore, although there is nothing prohibiting a government from borrowing to finance capital costs, the obligations arising out of such borrowing, such as regular interest payments, impact the expenditure side of deficit reduction in the same manner as current expenditures.

TELs were an extremely popular means of budgetary restraint in the late 1970s and 1980s. During the six year period from 1976 through 1982, 19 states enacted TELs. [187] Subsequent analysis has revealed that their impact on state revenue and expenditure growth has been quite limited.[188] Among the explanations frequently cited for TEL's lack of effectiveness include the existence of ambiguously drafted escape clauses such as those that permit the declaration of a "fiscal emergency", the exclusion of certain expenditures from the TEL requirements and artificially high base levels established at the time of the TEL enactment.[189]

The experience in the U.S., at both the federal and state levels, provides several important lessons for Canadians. First, penalty provisions, such as those established in GRH 1985 must be comprehensive in order to have the impact anticipated. Second, legislation that focuses solely on expenditures is likely to prove ineffective where the primary goal is deficit reduction. Third, provisions that are inflexible, such as many state constitutional requirements, or provisions that are excessively flexible or ambiguous, such as some TELs, are likely to be ignored or circumvented rendering the legislation ineffectual.

B. *European Union*

Although rarely characterized as balanced budget legislation, the *Treaty on European Union*, commonly referred to as the Maastricht Treaty,[190] includes deficit reduction provisions that are extremely influential. In particular, Article 104c contains very specific criteria that must be met in order for member states to join the European Monetary Union (EMU), scheduled to occur later this decade. The criteria established by Article 104c have recently been the focus of several European countries' fiscal policies, manifested by the radical new budgets that were proposed in Italy and Spain

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[185] J.V. Hagen, "A Note on the Empirical Effectiveness of Formal Fiscal Restraints" (1991) 44 J. of Pub. Econ. 199.

[186] D.R. Kiewiet & K. Szakaly, "Constitutional Limitations on Borrowing: An Analysis of State Bonded Indebtedness" (1996) 12 J. Econ. & Org. 62.

[187] *Supra* note 181 at 224.

[188] See, *e.g.*, *supra* note 176; Bails, *supra* note 181.

[189] *Supra* note 181 at 235-6.

[190] *Treaty on European Union (Maastricht Treaty)*, 7 February 1992.

in September 1996.[191]

Article 104c (1) establishes what is generally regarded as a policy statement by providing that "Member States shall avoid excessive government deficits".[192] Article 104c then stipulates reasonably specific criteria defining the meaning of "excessive". Specifically, the article provides that the European Commission monitor compliance with budgetary discipline and identify instances where state deficits exceed 3 percent of GDP or where net government debt exceeds 60 percent of GDP.[193] Article 104c also establishes a detailed procedure under which a member state may be fined or otherwise disciplined for violation of the deficit provisions.[194]

The specificity of the Maastricht Treaty deficit provisions has been the subject of considerable controversy and criticism.[195] For instance, several economists have noted that there is no magic to the 3 percent and 60 percent figures. Rather, the deficit ratio is slightly below the 1991 EC average of 4.3 percent and the debt ratio is close to the 1991 EC average of 61.7 percent, the time period during which the Maastricht Treaty was being negotiated.[196] Interestingly, the impetus during the negotiations for the strict criteria came from fiscally weaker countries such as Italy and Greece, which had traditionally run higher budget deficits.[197] This fact should come as little surprise, however, as those governments, who often found it difficult for domestic political reasons to rein in public spending, were anxious to gain external support for more restrictive economic policies.[198]

In view of the recent attention paid to the deficit provisions of the Maastricht Treaty, it would appear that the drafters have succeeded in achieving their goal. The advantage of EMU membership provides a vivid illustration of the power of a genuine penalty clause since many member states perceive the right to join the EMU is perceived by many member states as an absolute necessity and, therefore, the deficit provisions are being closely monitored and, where possible, adhered to.[199]

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[191] See, *e.g.*, "Guess Who's Coming to EMU", *The Economist* (5 October 1996) 47-8; F. Barton, "Focus: Spain'sBudget Seen Falling Short of Deficit Target" *AFX News* (30 September 1996); "Italy's Visco Says Gov't Raised Budget Deficit Cuts to Avoid Exclusion From EMU" *AFX News* (30 September 1996).

[192] *Supra* note 186 Article 104c (1).

[193] *Ibid.* Article 104c (2). Article 1 of the *Protocol on the Excessive Deficit Procedure*, attached to the Maastricht Treaty, contains the specific percentage figures.

Note, however, that the article provides some degree of flexibility. In particular, the article allows for an exception where a state deficit or debt ratio "is sufficiently diminishing and approaching the [debt or deficit ratio] at a satisfactory pace." "Satisfactory" is not defined and is left to the discretion of the European Commission.

[194] *Ibid.* Article 104c (3) - (14).

[195] In fact, given the stringent requirements prescribed by the Treaty, several EU countries are reportedly campaigning for a delay in the criteria's implementation. "Can EMU Be Left To Stew" *The Economist* (8 March 1997) 81.

[196] W. Buiter, G. Corsetti & N. Roubini, "Excessive Deficits: Sense and Nonsense in the Treaty of Maastricht" (April 1993) 16 Econ. Policy 58 at 62.

[197] M.J. Baun, *An Imperfect Union: The Maastricht Treaty and the New Politics of European Integration* (Boulder: Westview Press, 1996) at 70.

[198] *Ibid.*

[199] "Deficit Cuts, Southern Style" *The Wall Street Journal-Europe* (4 October 1996) 10.

C. *New Zealand*

Although much smaller economically than either the U.S. or the E.U., New Zealand's experiences with balanced budget legislation are nevertheless also worthy of examination. New Zealand has undergone significant monetary and fiscal reform in recent years, resulting in what some have characterized as "probably the best framework for monetary and fiscal policies...anywhere in the world".[200] The accolades are generally directed toward the *Fiscal Responsibility Act 1994*,[201] legislation that seeks to increase the openness and accessibility of the budgetary process and to provide politicians with incentives to pursue policies beneficial to the country's long-term interests.

The FRA includes several provisions of interest to Canadians. First, the Act requires the government to "pursue its policy objectives in accordance with the principles of responsible fiscal management".[202] Principles of responsible fiscal management are defined to include reducing total Crown debt to prudent levels,[203] achieving levels of Crown net worth that provide a buffer against future adverse economic events and pursuing policies that are consistent with a reasonable degree of predictability regarding the level and stability of tax rates for future years.[204] The FRA permits departure from the aforementioned principles in the event that such a departure is temporary and that the reasons for, and anticipated duration of, the departure are specified.[205]

In addition to the requirement to follow prudent policies, the FRA also establishes comprehensive disclosure requirements. For example, under the Act, the government is required to table: an annual budget policy statement indicating the government's long-term fiscal objectives;[206] an annual fiscal strategy report indicating the government's compliance with its long-term fiscal objectives;[207] an annual economic and fiscal update describing the fiscal forecasts for the following three years;[208] a semi-annual economic and fiscal update providing information on the current year;[209] a pre-election economic and fiscal update ensuring that there is no pre-election adjustment of the country's financial records;[210] and a current-year fiscal update indicating the previous year's fiscal performance.[211]

New Zealand's reforms, while not revolutionary, have two particularly impressive elements. First, the FRA establishes very stringent economic goals and does so in a manner that allows for flexibility. Although some may suggest that the impact of the

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[200] "The Great Escape", *The Economist* (1 April 1995) 60 [hereinafter "Great Escape"].

[201] *Fiscal Responsibility Act 1994*, 1994, No. 17 [hereinafter FRA].

[202] *Ibid.* at s. 4(1).

[203] "Prudent levels" are defined as a ratio of debt-to-GDP of below 30 percent in the short term and 20 percent in the long-term, far below those established by the Maastricht Treaty. *Supra* note 196.

[204] *Supra* note 197 at s. 4(2).

[205] *Ibid.* at s. 4(3).

[206] *Ibid.* at s. 6.

[207] *Ibid.* at s.7.

[208] *Ibid.* at ss. 8-10.

[209] *Ibid.* at s. 13.

[210] *Ibid.* at s. 14.

[211] *Ibid.* at s. 15.

reforms is lessened by their flexibility, the drafters appear to have recognized the ease with which excessively strict statutes are subject to amendment or repeal and have therefore enacted legislation that is more likely to survive intact in the long-term. Second, the level of disclosure mandated by the FRA is extremely significant. The legislation ensures the avoidance of temptations such as pre-election tax cuts or spending are avoided and thereby provides ample evidence of the benefits of an open, non-secretive approach to fiscal planning.

V. RECOMMENDATIONS FOR CANADIAN JURISDICTIONS

Having examined the recent Canadian balanced budget legislative experience and that of several other jurisdictions, the article now endeavours to synthesize those experiences into a series of practical recommendations. As suggested in the introductory discussion, the merit of balanced budget legislation appears to lie somewhere between the unqualified support of its advocates and the skepticism of its detractors. The extent to which a particular balanced budget statute is beneficial and effective will depend largely upon whether the legislation is truly a bona fide attempt at deficit reduction (rather than pre-election posturing) and the degree of incorporation of the following four criteria, all of which form the foundation for an effective piece of balanced budget legislation.

A. *The Need for a Balanced Approach*

The experience in Canada and elsewhere strongly suggests that deficit reduction cannot be accomplished by focusing solely on expenditures. Rather, a balanced approach that accounts for both spending and revenues is an absolute pre-requisite for a balanced budget statute to have an impact on deficit reduction. Unlike the spending limitation legislation in which deficit reduction was one of several legislative goals,[212] the primary goal of a balanced budget statute must be deficit reduction. The federal and Alberta Spending Control Act, the Nova Scotia ECA, and the experience at both the federal and state levels in the U.S. provide ample evidence of the fallacy focusing solely on the expenditure side of the ledger can control deficit spending.

A balanced approach to balanced budget legislation includes more than just accounting for both revenues and spending, however. As evidenced by the spending limitation legislation in Canada and GRH 1985 in the U.S., balanced budget statutes must avoid the creation of exempt expenditures or revenues. For example, several Canadian statutes exempted debt payments from the expenditure calculation. Similarly, GRH 1985, both in its original and amended versions, exempted a significant portion of annual expenditures by leaving permanent appropriations untouched. The result was a distorted and unrealistic picture of the fiscal health of the government and a diluted impact on deficit reduction. Balanced budget legislation must, therefore, address expenditures and revenues, with a minimal number of exceptions, in order to maximize its potential effectiveness.

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[212] The stated goals of spending limitation legislation typically include capping program spending. Deficit reduction is often perceived as an ancillary goal.

B. *The Need for Flexibility*

Although a flexible statute may seem to be at cross-purposes with the need for the balanced and comprehensive coverage and penalty provisions advocated herein, the power of a legislature to amend or repeal legislation that has become unduly burdensome must not be overlooked. Canadian constitutional law ensures that, with the exception of manner and form requirements, most balanced budget legislation can be amended or repealed. Moreover, politicians are unlikely to comply with balanced budget legislation whose effect would be sufficiently politically damaging as to exceed the political damage resulting from non-compliance with the legislation.[213] The experience in Canada, where Alberta and British Columbia repealed highly touted legislation less than one year after their enactment, demonstrates the ease with which "binding" legislation may be altered. Accordingly, balanced budget legislation must include sufficient flexibility to ensure that the legislation is strict enough to impact fiscal policy, yet flexible enough to adapt to unforeseen fiscal and economic changes.

The appropriate degree of flexibility may often be difficult to gauge. For instance, some analysts may regard the New Zealand approach as ineffective due to its excessive flexibility. However, the perils of excessively strict legislation are found throughout the U.S. where numerous balanced budget statutes have been ignored or circumvented on account of the political and/or economic impracticality of their provisions.

One method of establishing increased flexibility is to avoid the use of actual dollar targets within the legislation. As evidenced by the E.U. approach, targets expressed in percentage terms may have the same impact as dollar figures yet they have the distinct advantage of being able to account for the relative health of the overall economy. For example, a deficit target of $1 billion dollars may seem appropriate in year one, however, three years later it may be unrealistic or ineffectual as a result of economic changes that have transpired during the intervening years. However, if the deficit target is expressed as a percentage relative to the size of the economy, for example a deficit figure of 3 percent of GDP, the target stands a better chance of retaining its applicability, notwithstanding the economic changes.

Similarly, use of a generous time frame, such as the four year requirements established in Saskatchewan, may enable a government to alter its approach during particularly difficult fiscal times. The approach found in Manitoba's and Alberta's current legislation, in which balanced budgets are mandated on an annual basis, may result in politicians engaging in budgetary gymnastics, as experienced in several U.S. states, in order meet both the needs of the statute and the needs of their constituents.

Supermajority voting, which several U.S. states employ, is another means of creating increased flexibility. Such a mechanism ensures that balanced budget requirements remain in force subject to exceptional circumstances. In such instances, the legislature is free to override the legislation by the use of supermajority voting, which, in itself, may evidence widespread approval for the action since supporters of the proposed amendment must obtain a broad based coalition to ensure passage. Furthermore, supermajority voting has the additional appeal of being construed as a manner and form requirement and, therefore, binding on subsequent governments.

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[213] The consequences of non-compliance are relatively minor as they often entail an admission of failure to meet a political commitment, an unpalatable but not uncommon event.

C. *The Need for Penalty Provisions*

In view of the ease with which balanced budget legislation may be amended or repealed, establishing credibility is among the most challenging elements of a successful statute. Among the most effective means to establish this is the presence of a genuine penalty provision. Genuine and effective penalty provisions play an invaluable role in balanced budget legislation as they enable politicians to "blame" difficult spending cuts on the law. Moreover, such provisions provide an important enforcement mechanism that helps to ensure that policy makers abide by the governing legislation.

The penalty provision currently in force in the E.U. is likely as powerful a penalty provision as can be envisioned. The threat of exclusion from the EMU has left European leaders with no practical alternative other than to comply with the deficit reduction provisions.[214] Simultaneously, however, the existence of such a goal has enabled government leaders to credibly rally public support for the cuts or, alternatively, blame the E.U. for the hardships incurred on the domestic front.

The examination of balanced budget statutes provides other examples of effective penalty provisions. Manitoba's adoption of pay cuts to government ministers for non-compliance with its balanced budget legislation provides Canada's strongest penalty provision. A more effective, yet highly unlikely penalty provision, would require a government to resign and call a general election in the event of non-compliance with its balanced budget legislation. Alberta rejected such an approach in 1993 and it would likely meet the same fate in most jurisdictions. Finally, the sequestration process of GRH 1985, which ultimately failed in its intended impact, could prove to be an effective penalty provision with the elimination of the exclusions that hampered GRH 1985 were eliminated. Drafting an effective penalty clause is a politically risky endeavour; however, the reward may well be a degree of statutory credibility and effectiveness that is otherwise unattainable.

D. *The Need for Openness*

One of the most positive by-products of the recent surge in balanced budget legislation has the been the increased level of openness and disclosure of the budgetary process. Prior to this recent development, the budgetary process was often characterized by its highly secretive nature. Although this arose out of concern for the possible unfair use of undisclosed information, several unwanted side effects also resulted. In particular, the primacy of retaining secrecy resulted in limited consultation with industry and economic leaders prior to a budget's introduction and, thereby, increased the likelihood of market surprise. Furthermore, the secrecy surrounding budgetary data increased the possibility of budgetary manipulation through exaggerated forecasts, particularly during election periods.[215]

Most of the balanced budget statutes examined establish increased disclosure requirements. Many require semi-annual or even quarterly reports of government spending and revenues; reports on progress toward deficit and debt reduction targets; and projections based upon conservative economic estimates. Such provisions are to

[214] Although given the difficulty of compliance, some are now campaigning to delay implementation of the criteria. *Supra* note 191.

[215] *Supra* note 147.

be welcomed as they better inform the public about budgetary issues, reduce the likelihood of surprise in the financial marketplace and, in doing so, increase political accountability.

Moreover, as demonstrated in New Zealand, increased information availability can also result in increased credibility. Stringent disclosure requirements lessen the opportunity for questionable pre-election activities and increase political accountability. Those jurisdictions that have not adopted comprehensive disclosure requirements, such as the tabled Quebec Act, should contemplate incorporating the necessary amendments to increase their level of disclosure in an effort to improve the overall quality and effectiveness of their balanced budget legislation.

VI. CONCLUSIONS

The rapid rise in popularity of balanced budget legislation in Canada has provided a strong indication of the public's growing interest in governmental fiscal policies and in the pursuit of fiscally "prudent" objectives. Although dismissed by critics as little more than policy statements posing as legislation, the development of such legislation in Canada shows clear signs of seriousness of purpose and genuine desire to impact on spending decisions.

The initial balanced budget statutes, which were generally in the form of spending limitation legislation, such as those enacted federally and in Alberta and Nova Scotia, suffered from several shortcomings. These included a lack of balance given the exclusive focus on expenditures, a lack of accountability given the absence of penalty provision, and the presence of numerous loopholes rendering the statutes ineffective.

Subsequent legislative initiatives in Canada took the form of balanced budget legislation. The initial attempts at balanced budget legislation, such as those statutes enacted in B.C. and New Brunswick, also proved problematic. Those attempts included significant loopholes such as the absence of enforcement mechanisms and the exclusion of important revenues or expenditures in the balanced budget calculation.

The more recent balanced budget statutes, particularly those found in Alberta, Saskatchewan and Manitoba, have made significant improvements. Legislators have increasingly recognized the need for a balanced approach that accounts for all revenues and expenditures in the calculation of the deficit, the need for penalty provisions to ensure enforcement of the statute and the need for flexibility to enable policy makers to adapt to changing economic conditions.

Notwithstanding the positive changes in the Canadian legislation, there remains room for improvement. The experiences of foreign jurisdictions reinforce the effectiveness of genuine penalty provisions, the tendency of politicians to evade statutory provisions lacking in flexibility, and the benefits of comprehensive disclosure of the budgetary process.

The recommendations outlined in Part V, including the need for a balanced approach, the need for flexibility, the need for penalty provisions, and the need for openness, demonstrate the difficulty of devising balanced budget legislation that fully achieves its stated objectives. This difficulty may be due to the fact that although there may be tangible benefits to balanced budget legislation, the harsh reality is that difficult decisions cannot be delegated to a statute. Experience provides ample evidence of the hardships budgetary cutting inflicts. Unfortunately, much as some political leaders

might try to avoid it, there are no simple or easy means to circumvent such decisions. While balanced budget legislation may provide assistance, it cannot replace strong political leadership.[216]

The experience in Canada and elsewhere suggests that deficits and debt can be cut or controlled with or without balanced budget legislation. Balanced budget legislation can play an effective role in disclosing governmental objectives, keeping policy makers focused on their stated fiscal objectives and increasing the level of public awareness and participation. However, without leadership to make the difficult choices, to convince the public of the necessity of deficit reduction, and to comply with both the letter and spirit of such legislation, balanced budget statutes are destined to be wholly ineffective. Therefore, while politicians may extol the benefits of balanced budget statutes, their effectiveness will depend largely on the leadership and commitment to fiscal discipline of those same politicians.

[216] A 1994 U.S. study of six countries' experiences with balanced budget legislation concluded that the key role in fiscal policy is not balanced budget requirements, but rather leadership that defines the benefits of deficit reduction and emphasizes themes that find broad public support. *Supra* note 146 at 8.