Office of the Auditor General of Nova Scotia

# Chapter 3
# Nova Scotia's Finances from the 2022 Public Accounts

## Key Messages

- Nova Scotia's economy and finances are rebounding to pre-COVID-19 levels
- 2021-22 operating surplus of $351 million
- Net debt to GDP ratio of 32.2% below pre-pandemic level
- Federal transfers as a percentage of total revenues remain at the top of the five-year trend but improved over 2020-21

## Why We Did This Chapter

- To provide important information to Nova Scotians on the Province's finances and promote discussion

**Financial Condition of the Province of Nova Scotia**

Government's financial condition can be assessed by ratios and indicators of sustainability, flexibility, and vulnerability. These indicators are suggested by Canada's CPA independent Public Sector Accounting Board.

Sustainability indicators show the Province's ability to maintain existing services and financial requirements without needing to increase revenues or debt

- 2021-22 operating surplus of $351 million driven by increased revenues following a deficit in 2020-21
- Net debt increased to $16.6 billion since 2017-18 but rate of growth year over year is back to pre-pandemic levels
- Net debt to GDP ratio of 32.2% in 2021-22 is below pre-pandemic levels
- Actual borrowings were less than budgeted in 2021-22 but unmatured debt increased by $35 million to $14.85 billion and remains on the high end of the five-year trend
- Overall: while indicators have fluctuated over the past five years, operating surplus and net debt to GDP have improved over 2020-21

Flexibility indicators show the Province's ability to increase revenues or debt borrowings within its economy

- Interest on unmatured debt has decreased from 2017-18 levels, specifically by $51 million to $576 million in 2021-22 compared to the prior year, and a five-year low
- In 2021-22 provincial source revenue to GDP ratio increased by 1.3 percentage points to 17.7% but is still relatively stable from years prior
- Overall: flexibility indicators have shown improvement in the Province's ability to increase debt borrowings within its economy

Vulnerability indicators show the Province's reliance on revenues outside of its control

- Dependency on federal government transfers increased over past five years to 35.2% in 2021-22
- Overall: federal transfers as a percentage of total revenues improved over the prior year but remain at the high end of the five-year trend

**Selected Financial Highlights**

Revenue:

- At $9.1 billion, provincial source revenue was $961 million higher than budget with $389 million resulting from prior year adjustments
- Personal income tax revenue of $3.1 billion was higher than both the budget and prior year amounts, and has risen 13% since 2017-18
- Harmonized sales tax revenue of $2.1 billion was higher than both the budget and prior year amounts and has risen 16% since 2017-18
- Corporate income tax revenue of $518 million rebounded from 2020-21 but remains on the low end of the five-year trend
- Net income from government business enterprises of $406 million is the peak of the five-year trend

## Questions Nova Scotians May Want to Ask

1. Why was the 2021-22 ending surplus so much more than expected?
2. What does the decrease in net debt to GDP ratio mean for me?
3. Personal income tax and harmonized sales tax revenues have both increased over the past five years whereas corporate income tax has not. Why is this?
4. What will happen to the Province's interest payments as rates go up?

# 3 Nova Scotia's Finances from the 2022 Public Accounts

## Purpose

3.1 The purpose of this chapter is to inform Nova Scotians on some aspects of the Province's finances and to promote discussion.

3.2 In this chapter, we look at numbers from the perspective of sustainability, flexibility, and vulnerability and provide information on the current level of revenues against levels over the previous five years to provide insight into the Province's financial condition.

## Limitations

3.3 We are not assessing or commenting on the financial decisions made by Government or the effectiveness of those decisions. The information presented below is only part of the story and does not consider such factors as policy decisions, actual programs and services, inflation, performance of the provincial economy, and other elements that may impact revenues and expenses. Certain figures and information in this report including information on entities not consolidated in the Province's financial statements is not audited. Additional information, including economic highlights, is presented in the Financial Statement Discussion and Analysis section in Volume 1 of the 2022 Public Accounts of Nova Scotia where there are almost fifty pages of detailed analysis and explanation.

## Financial Indicators – What They Show

### Some indicators returned to pre-pandemic levels

3.4 There are various indicators that can be used to assess the Province's financial condition. The indicators included in this chapter are among those recommended for reporting by the Public Sector Accounting Board's Statement of Recommended Practice – 4: *Indicators of Financial Condition*. The indicators reported are meant to provide additional information on the Province's financial condition but are not intended as commentary on the financial impact of government policies or fiscal management.

3.5 The Statement of Recommended Practice recommends that, at a minimum, indicators related to sustainability, flexibility, and vulnerability be considered. We have included these types of indicators, along with other information we feel is useful in demonstrating the Province's financial condition. These tools can assist users of the Province's consolidated financial statements to interpret its financial information.

3.6 The financial indicators presented in this chapter provide an overview of the Province's financial performance for the five-year period ending March 31, 2022 and are summarized in the table below as well as in the 2021-22 Public Accounts.

| Financial Highlights | |
|---|---|
| **Indicator** | **Five-Year Trend** |
| **Sustainability** | |
| Annual surplus or deficit | Improved |
| Net debt | Worsened |
| Net debt to GDP | Improved |
| Budget to actual borrowing requirements | Fluctuated |
| Unmatured debt | Worsened |
| **Flexibility** | |
| Interest on unmatured debt | Improved |
| Own source revenue to GDP | Improved |
| **Vulnerability** | |
| Federal government transfers as a percentage of total revenue | Worsened |

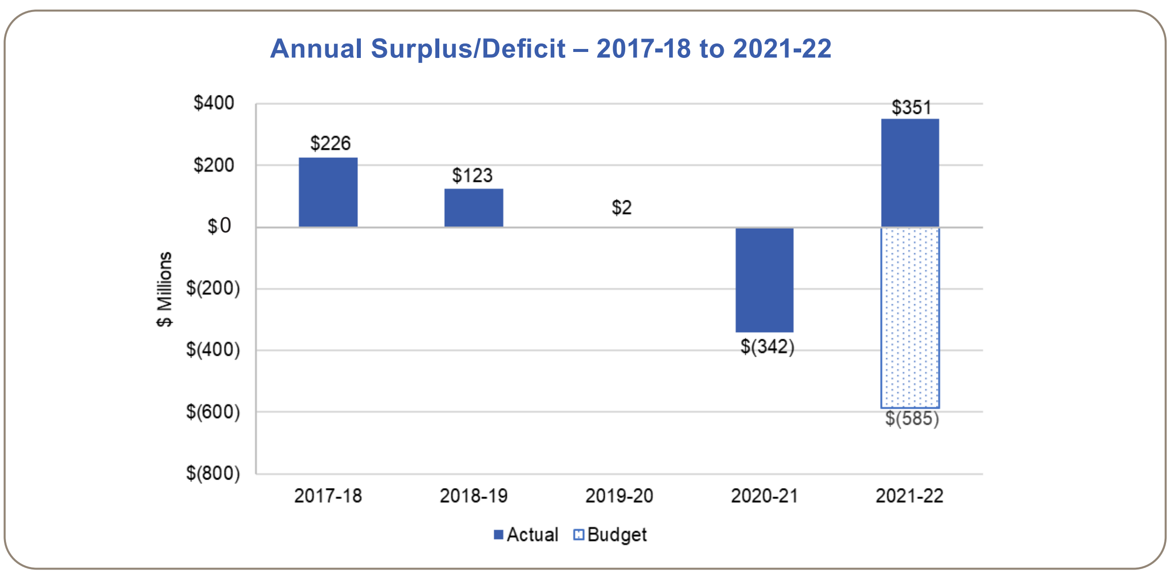
3.7 Individual sustainability indicators show a range of impacts on sustainability. Based on the indicators reported, the results also show the Province's flexibility has improved but it appears to be more vulnerable as it relies more on federal revenues.

## Sustainability

3.8 Sustainability measures the ability of a government to maintain its existing programs and services, including maintaining its financial obligations to creditors, without having to increase debt or tax rates. Sustainability indicators provide insight into how a government balances its commitments and debts.

### The Province reported an annual operating surplus of $351 million for 2021-22

3.9 The annual surplus/deficit measures the extent to which revenues cover expenses. A surplus occurs when revenues are greater than expenses. A deficit occurs when expenses are greater than revenues.




*Source: 2021-22 Public Accounts*

3.10 Reported results in 2021-22 show significant improvement over both the initial 2021-22 budget estimates and the 2020-21 actuals. The resulting surplus of $351 million was $936 million higher than the budgeted deficit of $585 million and $693 million higher than the prior year's deficit of $342 million. This was the largest budget to actual change in surplus in the past 20 years.

3.11 The large swing from budgeted deficit to actual surplus was mainly driven by a $961 million increase in Provincial source revenues including:

- Increase in major tax revenues of $272 million from budget:

  - Personal income tax revenue increased $179 million
  - Harmonized sales tax revenue increased $75 million
  - Corporate income tax revenue increased $18 million

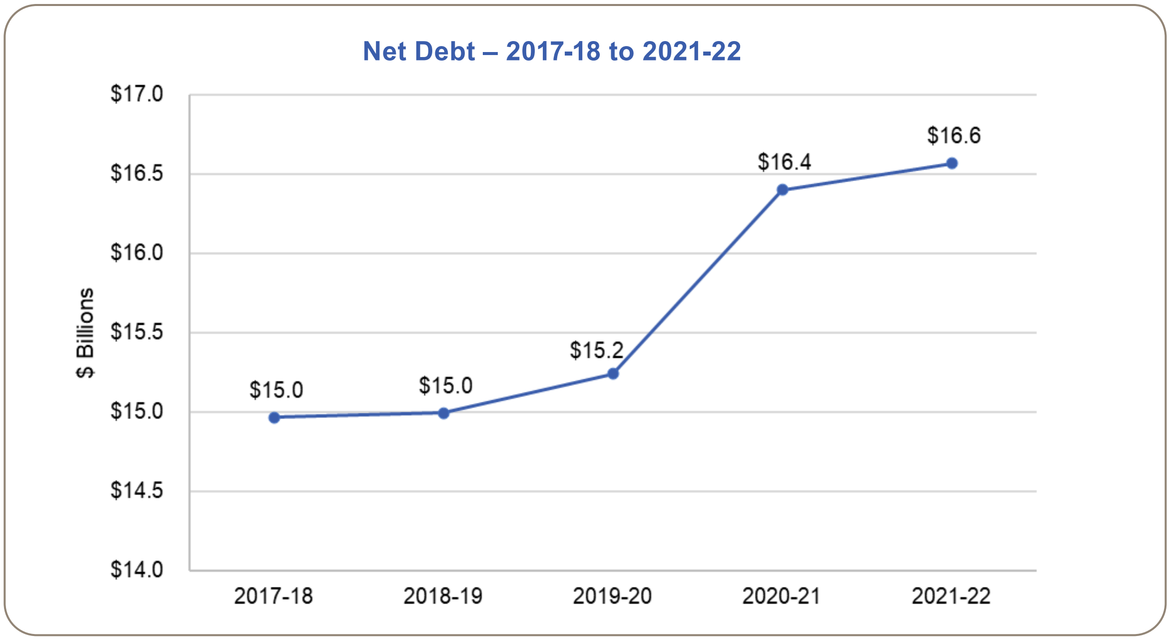
  These increases were mainly as a result of the Provincial economy rebounding stronger than anticipated; higher taxable income and projected yield rates; and greater residential housing investment and consumer expenditures.

- Prior year adjustments (PYAs) of $389 million added to major tax revenues. Prior year adjustments are not budgeted. They are recorded in the current year as actual or more current information becomes available and impact the accounting estimates for tax revenues recorded in prior years. Prior year adjustments are discussed in further detail later in this chapter.

- Offshore license forfeitures of $125 million. Offshore license forfeiture is not unusual given the unpredictable nature of the offshore industry. The Province records forfeiture revenue when a notice of forfeiture is given by a license holder. Offshore license forfeitures are not budgeted because the amount and timing cannot be reasonably predicted. Revenue in 2021-22 was from forfeiture of exploration licenses from BP Canada and Equinor Canada.

## The Province's net debt increased $1.6 billion since 2017-18

3.12 Net debt measures the degree to which the Province's financial assets cannot cover its liabilities. As the chart below shows, net debt was fairly stable at approximately $15 billion prior to the pandemic. It increased significantly in 2020-21 to $16.4 billion but has returned to pre-pandemic year-over-year growth levels and was $16.6 billion at the end of 2021-22.



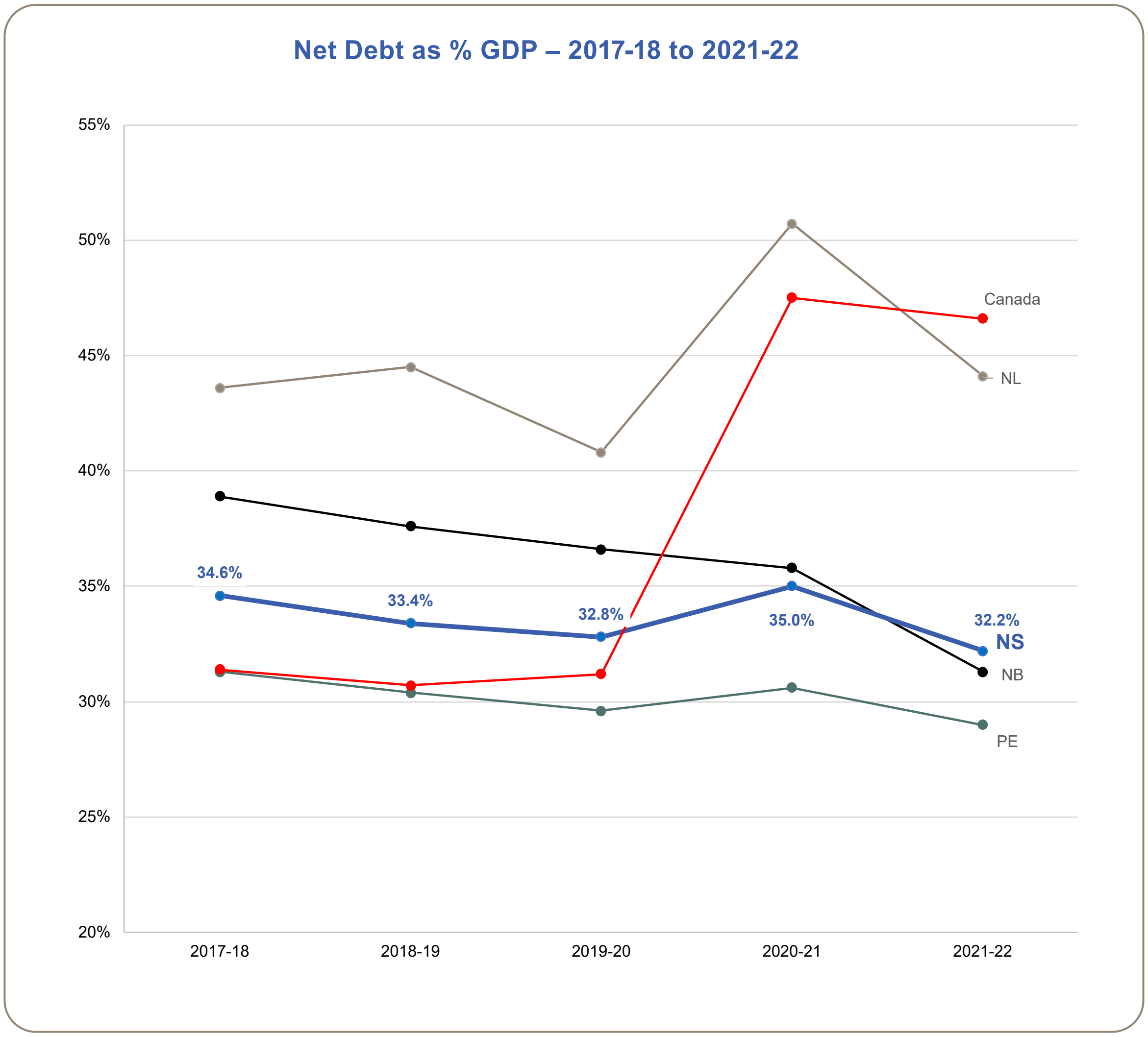

*Source: 2021-22 Public Accounts*

## The Province's net debt to GDP ratio is below pre-pandemic level

3.13 Gross domestic product (GDP) is the amount of value added from production of all goods and services within the Province in a given year, and is one of the primary measures used to evaluate the economic condition of a province or country.

3.14 The net debt to GDP ratio is used to assess the Province's ability to pay its financial obligations and render services. A low ratio indicates a level of economic output that supports debt repayment. The higher the ratio, the more difficult it may be for the Province to pay its debt while maintaining the same service levels.

3.15 The following chart shows that Nova Scotia's net debt to GDP ratio decreased over the past five years, except for 2020-21 which is when major impacts due to COVID-19 occurred. Net debt to GDP ratio was 32.2 per cent in 2021-22, which is below pre-pandemic levels.




*Source: 2021-22 Public Accounts and RBC Economics Canadian Federal and Provincial Fiscal Tables*

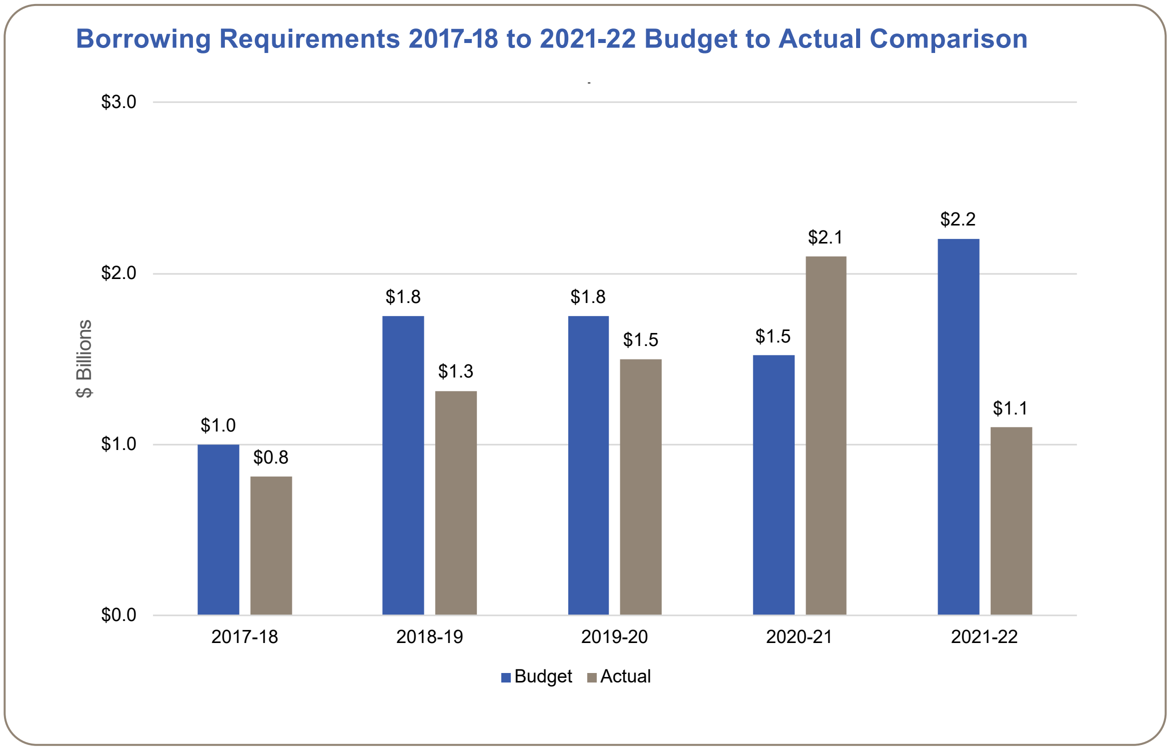
3.16 While the percentages are not strictly comparable between provinces due to accounting and reporting differences, the above chart shows Nova Scotia's net debt to GDP ratio against other Atlantic provinces and Canada to illustrate the trend that net debt to GDP peaked in 2020-21. All Atlantic provinces, except Newfoundland and Labrador, reported ratios below pre-pandemic levels in 2021-22.

3.17 The following paragraphs show the actual results of the Province's annual borrowing requirements and net unmatured debt.

## The Province's actual debt borrowings in 2021-22 were less than budgeted

3.18 The Province's annual borrowing program presented in the annual budget document represents the amount of new debt that can be issued in a fiscal year by the General Revenue Fund. In 2021-22, the Province borrowed $1.1 billion, which was $1.1 billion lower than the budgeted borrowing program. The $2.2 billion budget was released in March 2021 when there was great uncertainty in the midst of the COVID-19 pandemic and with consideration to the fact that the Province had borrowed $2.1 billion in 2020-21. The 2021-22 borrowings were comprised of 30-year and 10-year debentures at coupon rates between 2.00 and 3.15 per cent.

3.19 When the Province issues debt, it often does so in the domestic public market but maintains the ability to issue internationally. The Province sells its bonds to a syndicate, a group of investment dealers, primarily consisting of Canadian banks. The investment dealers then sell the bonds to investors, including Canadian pension plans, insurance companies, and banks.

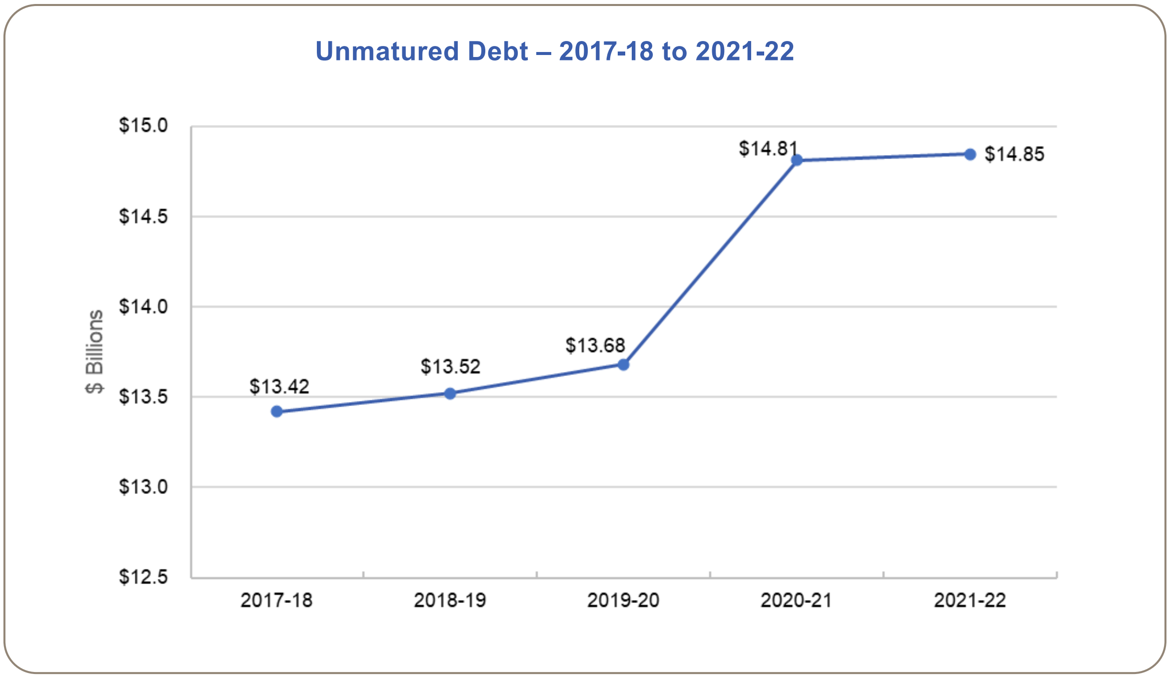



*Source: Public Accounts 2017-18 to 2021-22*

## The Province's unmatured debt increased by $35 million to $14.85 billion in 2021-22

3.20 The Province's unmatured debt is primarily made up of long-term debentures and various loans. It includes new debt issuances and those from prior years and is net of sinking funds.

3.21 Unmatured debt increased $35 million from $14.81 billion in 2020-21 to $14.85 billion in 2021-22 and has increased $1.43 billion since 2017-18.




*Source: Public Accounts 2021-22*

## Flexibility

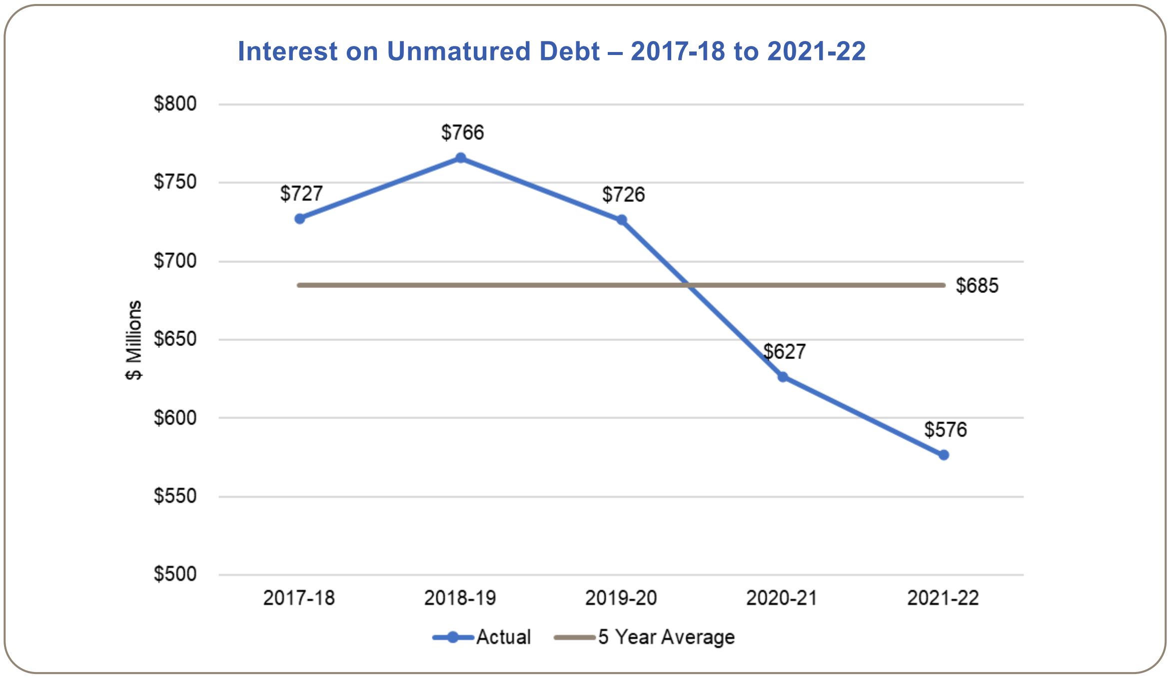
**The Province's annual interest on unmatured debt decreased $51 million in 2021-22**

3.22 Flexibility is the degree to which a government can change its debt burden or raise taxes within its economy to meet its existing financial obligations. Flexibility provides insights into how a government manages its finances. Increasing debt obligations and interest costs reduce a government's future flexibility and ability to respond to changing circumstances.

3.23 Interest on unmatured debt is the cost incurred by the Province to pay interest on outstanding loans, interest on the Province's unfunded pension and post-retirement benefit obligations, and other costs related to debt financing. Higher debt servicing costs mean the Province is using more of its revenue to pay for interest and is therefore not able to use that money to provide services or reduce taxation. Lower debt servicing costs allow the Province greater flexibility in meeting its service and financial commitments.

3.24 Despite unmatured debt increasing in the past five years, debt servicing costs decreased in 2021-22. This is due to high interest rate debt maturing in recent years.

3.25 The average amount of interest paid over the past five years was $685 million. The interest on unmatured debt for 2021-22 was $576 million; a decrease of $51 million from $627 million in 2020-21 and a five-year low.

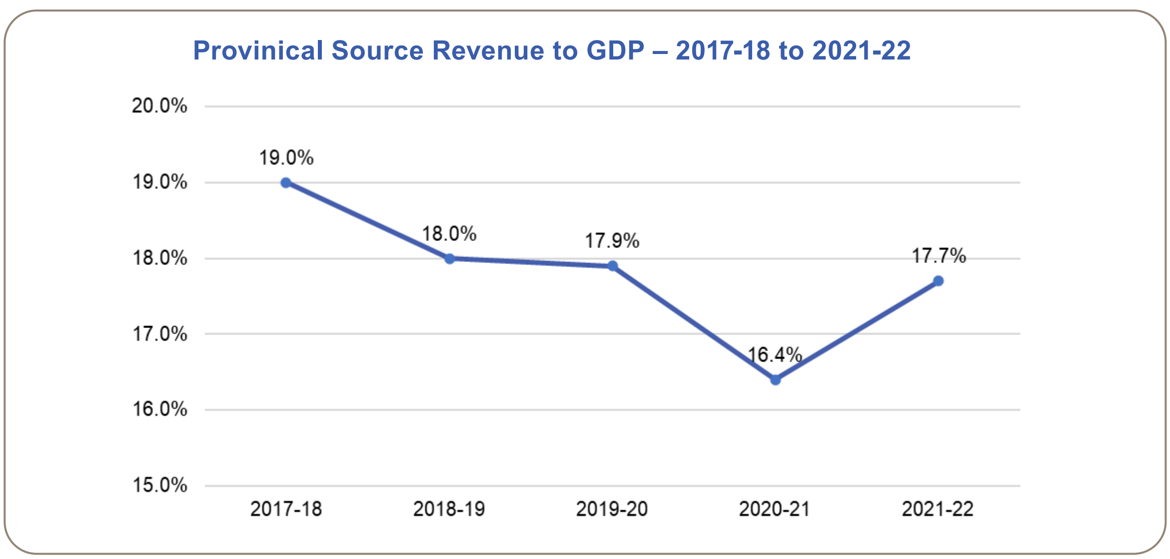



*Source: Public Accounts 2018-19 to 2021-22*

## Provincial source revenue to GDP increased to 17.7 per cent in 2021-22

3.26 Provincial source revenue as a percentage of GDP measures the extent to which the Province derives income from the provincial economy, either through taxation, user fees, recoveries, or other provincial revenues. Increases in this ratio suggest reduced flexibility and this indicator helps a government determine the extent to which it can access own source revenues in the future.

3.27 Provincial source revenue as a percentage of GDP increased to 17.7 per cent in 2021-22, which is 1.3 percentage points higher than 2020-21 but still relatively stable from the years prior. This is due to increases in revenue from taxes and other provincial sources.




*Source: 2021-22 Public Accounts*

## Vulnerability

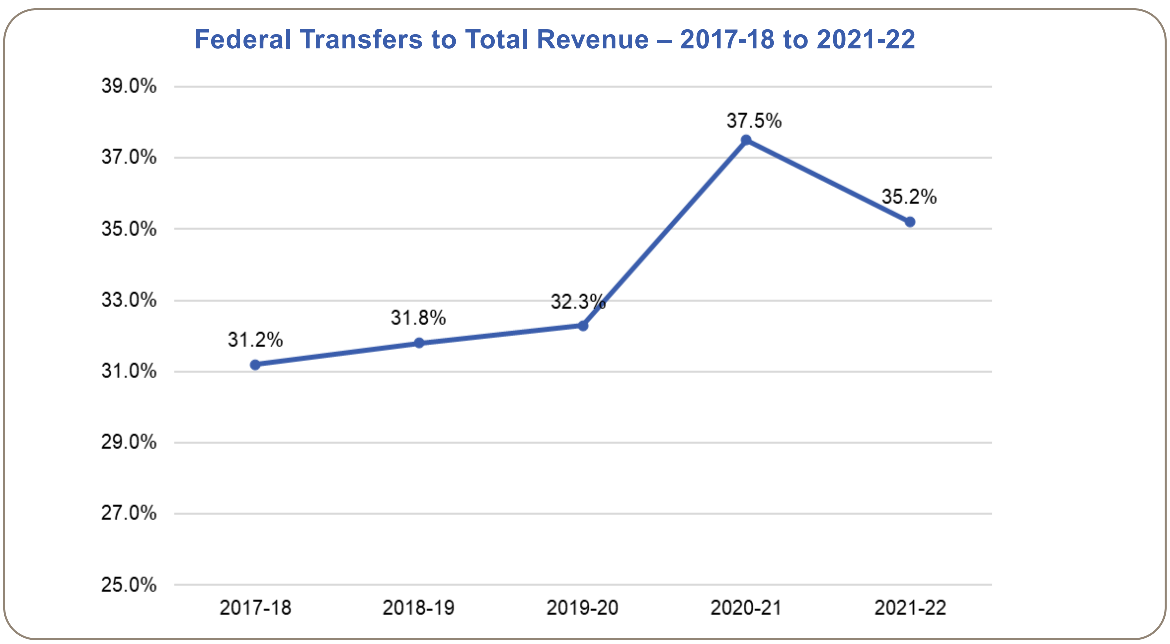
3.28 Vulnerability indicators measure a government's dependency on sources of revenue outside its control and its exposure to risks which might affect a government's ability to meet its commitments. The more a government relies on revenue from other sources, the more dependent it is on the fiscal decisions of others.

### Dependency on federal government transfers increased over the past five years

3.29 As illustrated below, Nova Scotia continues to rely on federal government equalization payments and other transfers. More than $1 in every $3 of the Province's revenue comes from the federal government.

3.30 Federal transfers as a percentage of total revenues decreased 2.3 percentage points to 35.2 per cent from its five-year peak of 37.5 per cent in 2020-21. This decline is attributable to provincial source revenue growing more than federal transfers. Provincial source revenue and federal source revenue both peaked in 2021-22.

3.31 Federal transfers increased in fiscal 2020-21 as a result of COVID-19 related funding received from the Federal Government. The Province reported total COVID-19 related federal revenue of $211 million in 2021-22 and $462 million in 2020-21.




*Source: 2021-22 Public Accounts*

## Revenue Highlights

3.32 The financial trends and comparisons presented below do not consider the impact that factors such as policy decisions, actual programs and services, inflation, and other elements have had on revenues.

## Provincial source revenue was $961 million over budget

3.33 The Province budgeted $8.155 billion in revenue from provincial sources in 2021-22. The actual revenue collected from provincial sources in 2021-22 was $9.116 billion, $961 million higher than budgeted.

3.34 A large portion of the nearly $1.0 billion in revenues over-budget is attributed to adjustments from prior year estimates. Prior years' adjustments are recorded as more current information becomes available. For example, the tax revenues for the year are estimated based on forecasting future economic and tax filing data since there is a delay in when the Province receives actual results (i.e., once personal tax returns are filed and assessed). Once actual filing data is received, the Province records a PYA for the difference between the original estimate and the most recent actual data. PYAs are generally recorded for personal income tax, corporate income tax, and harmonized sales tax revenues. The PYAs are not budgeted; therefore, the $389 million in PYAs recognized in 2021-22 resulted in revenues being over budget. PYAs from provincial sources are comprised of $183.4 million for personal income tax, $120.1 million for corporate income tax, $85.3 million for harmonized sales tax and were partially offset by a negative PYA of $0.1 million for large corporations tax.

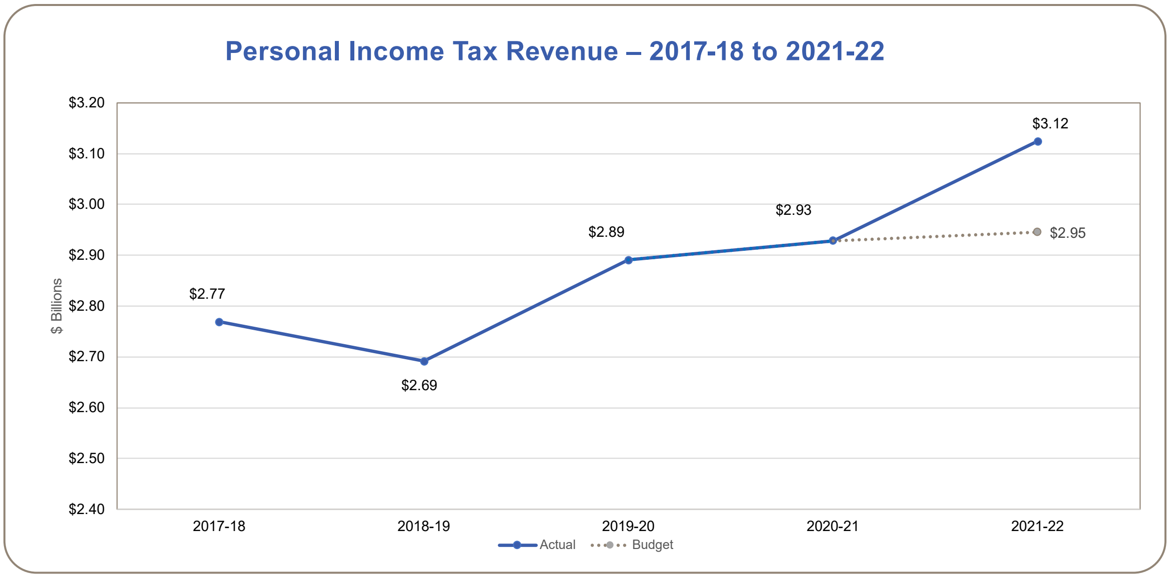
3.35 Four of the largest provincial revenue sources in 2021-22 were:

- Personal income tax – $3.1 billion
- Harmonized sales tax – $2.1 billion
- Corporate income tax – $518 million
- Income from government business enterprises – $406 million

## Personal income tax revenue was higher than both the budget and prior year amounts

3.36 Personal income tax revenue of $3.1 billion was the largest source of provincial revenue reported in 2021-22; higher than both the 2021-22 budget and 2020-21 actual amounts. It was $179 million higher than budget primarily due to higher taxable income and projected yield rates. Federal measures like the Canada Recovery Benefit (CRB), the Canada Recovery Sickness Benefit (CRSB), and EI Caregiving Benefit raised incomes in 2021-22. These measures were also responsible for most of the $200 million increase over prior year actuals.

3.37 Personal income tax revenue has risen by close to $350 million or 13 per cent since 2017-18.

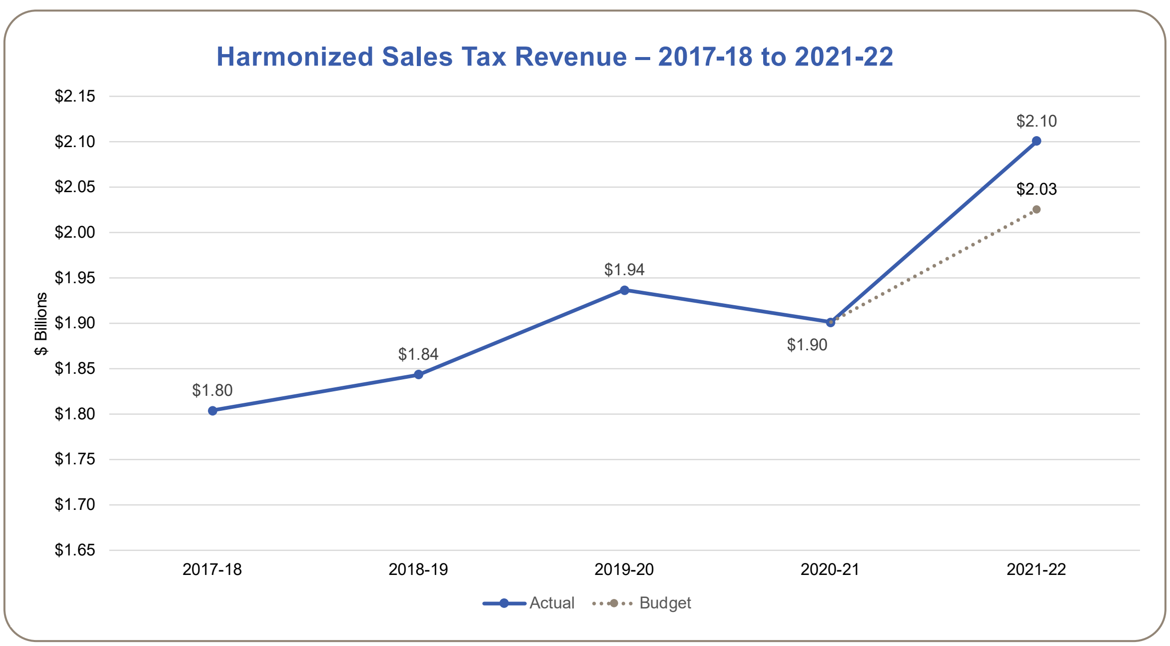



*Source: Public Accounts 2018-19 to 2021-22*

## Harmonized sales tax revenue exceeded both the budget and the prior year amounts

3.38 Harmonized sales tax revenue was $75 million higher in 2021-22 compared to the budget, primarily due to greater residential housing investment and consumer expenditures.

3.39 With the exception of lower taxable consumer expenditures resulting from the public health restrictions in place during the pandemic in 2020-21, harmonized sales tax revenue increased in each year since 2017-18 and has grown by $297 million or 16 per cent since 2017-18 to $2.1 billion in 2021-22.

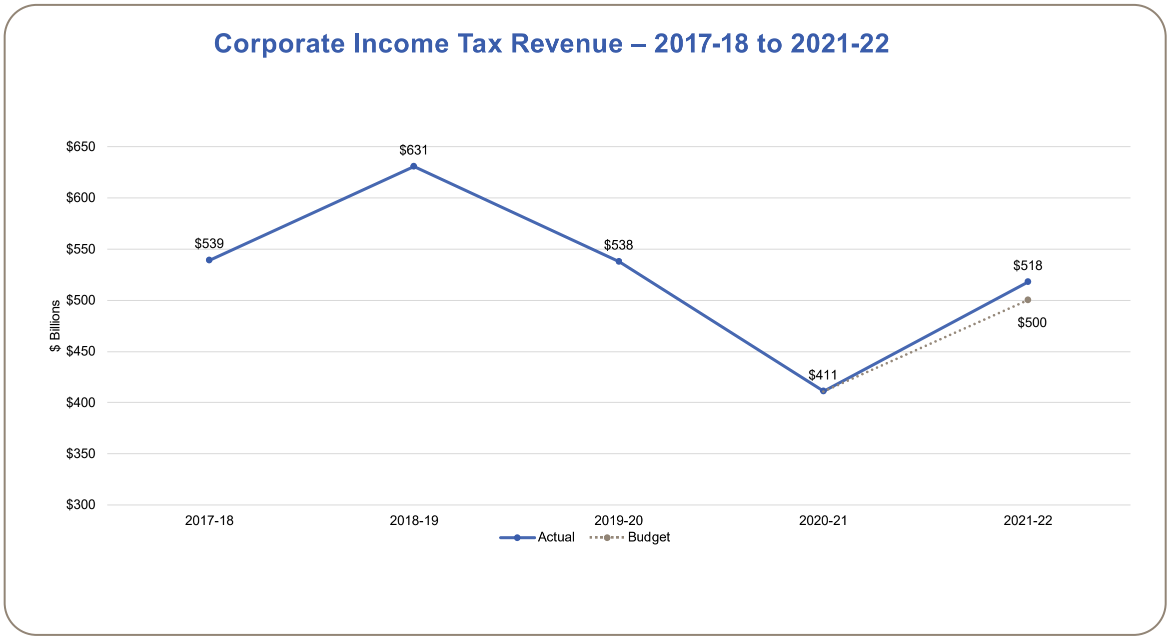



*Source: Public Accounts 2018-19 to 2021-22*

## Corporate income tax revenue rebounded from 2020-21

3.40 Corporate income tax revenue was close to $20 million higher than budget in 2021-22 due to increases in national taxable income offset by a decline in Nova Scotia's share of national taxable income and an increase in the small business share of taxable income.

3.41 Although actual corporate income tax revenue rebounded over 2020-21 actual results by more than $100 million, it is still lower than 2017-18. The decrease in corporate income tax revenues occurred primarily in fiscal years 2019-20 and 2020-21 due to negative impacts of COVID-19 on national corporate taxable income and the decline of the Province's share of national taxable income.




*Source: Public Accounts 2018-19 to 2021-22*

## Net income from government business enterprises of $406 million in 2021-22 is the peak of the five-year trend

3.42 Total net income from government business enterprises reached $406 million in 2021-22 and is comprised of the following:

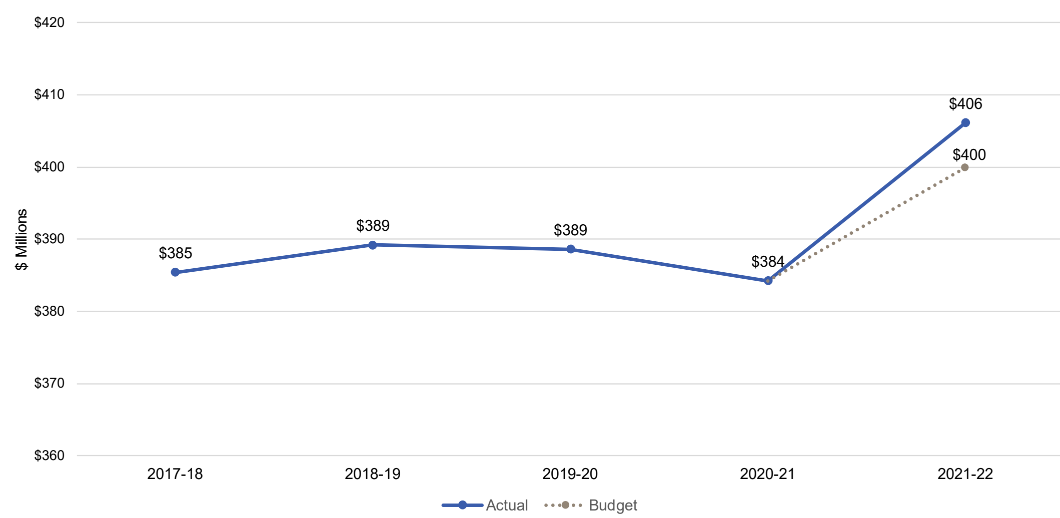
- Net income from Nova Scotia Liquor Corporation of $268.7 million. This represents a decline of $5.8 million from the prior year and is attributable to increased costs including wages and salary expenses for new cannabis stores. Although net income declined from 2020-21, it remains significantly above pre-pandemic levels.

- Net income from Nova Scotia Gaming Corporation of $130.0 million. This is $27.0 million higher than the prior year due to fewer COVID-19 restrictions. Although some restrictions remained through 2021-22 including reduced gaming capacity, limited food and beverage services, there were more operational days than the prior year, resulting in increased revenue.

- Net income from Halifax-Dartmouth Bridge Commission of $5.5 million. This is a $4.8 million increase over the prior year and is due to increased traffic volumes, including the return of traffic levels as COVID-19 restrictions eased, as well as a toll increase of 25 per cent in January 2022.

- Net income from Highway 104 Western Alignment Corporation of $1.9 million. This represents a decline of $4.1 million and is primarily attributable to toll exemptions for Nova Scotia registered vehicles beginning in December 2021.

**Net Income from Government Business Enterprises – 2017-18 to 2021-22**




*Source: Public Accounts 2018-19 to 2021-22*

3.43 The five-year high net income from government business enterprises (GBE) is attributable to increased net income from the Nova Scotia Liquor Corporation which increased by more than $30 million since 2017-18 while other GBEs had decreased revenues since 2017-18.