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From: Yves Giroux and Alexandre Laurin
To: Canadian Fiscal Observers
Re: FALL BUDGETS GOOD; NEW CAPITAL INVESTMENT DEFINITION BAD

The federal government recently announced two major changes to the way it manages and presents its finances: A new capital budgeting framework and a shift to fall budgets, with fiscal updates moving to the spring.

Moving budgets to the fall does make sense. But reclassifying spending through a new capital framework risks being more confusing than clarifying.

Ottawa's recent habit of **tabling budgets** in March, April or not at all has left parliamentarians approving annual expenditures – the main estimates – that don't line up with actual budget decisions. Because the main estimates must be tabled by March 1, MPs and senators often only get to vote on an incomplete picture of government spending.

A fall budget will help align budgeting with the parliamentary supply cycle. It will allow new spending measures to be reflected in the main estimates, giving legislators a more accurate view of spending before the fiscal year begins on April 1. It will also allow departments and government agencies, not to mention the provinces and territories, to plan better, as they will learn their resource levels several months before the start of their fiscal year, rather than finding out after they have crafted their own budgets.

The new **capital budgeting framework** is not such an obvious improvement.

The government says it will help Canadians “better understand how fiscal choices support future economic capacity.” In practice, it will simply reclassify some spending as “capital investment.”

Ottawa adopted accrual accounting more than two decades ago to spread the cost of its capital investments over their useful lives. Such assets already receive distinct accounting treatment in accordance with public sector accounting standards (PSAS). By contrast, with one exception the spending the government proposes to reclassify as “capital investment” will not correspond to any capital asset on the government's balance sheet, which is a major deviation from PSAS. (The exception is actual capital amortization; a relatively small item.)

Under the new definition, capital investment covers any spending or tax measure that contributes to capital formation even if another government or a private entity holds the assets. That includes infrastructure transfers, tax credits and deductions for business investment, amortization of federal assets, support for private-sector research and development, and measures to unlock private capital investment or accelerate housing supply.

Associating all such spending with specific assets would be very difficult: It would be nearly impossible for the federal government to keep an accurate tally of the “capital assets” held by businesses it has helped fund.

Spending that doesn't meet these criteria will be considered day-to-day operating spending. Examples include payments to seniors, child benefits, health and social transfers and the cost of running government.

The stated goal is to make it easier for Canadians to see how fiscal choices support long-term growth.

In fact, this framework will mainly muddy the water. By creating two bottom lines, one showing the deficit as we have become accustomed to calculating it, and another excluding so-called “capital investment,” the government will make its budgets harder, not easier, to read. Few Canadians are fluent in public-sector accounting, and adding another lens will blur rather than sharpen the fiscal picture.

Some spending the government proposes to call “investment” has only a tenuous link to capital formation. For instance, the GST rebate for first-time homebuyers is primarily a subsidy that boosts housing demand. How will the government measure how much new capital it and similar incentives result in?

Even worse are the tax credits and deductions the government proposes to count as capital investment. The value of investments such incentives generate is assumption-based and uncertain and they reduce revenue rather than increase spending. Treating foregone revenue like a productive investment is misleading. By that logic, if Ottawa were to eliminate the corporate income tax for a few years and consider it an “investment” – forfeiting more than \$85 billion a year in revenue – the operating deficit would shrink. That's absurd.

Whether an expenditure is labelled an “investment” or an “expense,” it must be financed by taxes or borrowing and it contributes to public debt and future interest costs. It is hard not to conclude the government is proposing this new framework mainly to justify higher spending.

True transparency comes from clear, consistent reporting and accounting based on recognized standards, not from re-labelling the budget figures to show a smaller deficit. In a year when the deficit is likely to exceed \$70 billion, the government's promise of greater transparency rings hollow. A fall budget may help align Parliament's expenditure approval process with accurate and complete intentions. But the new capital budgeting framework will reduce transparency and risks putting the federal government on a path to even higher debt.

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