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Overview of Contingent Liabilities



OFFICE OF THE PARLIAMENTARY BUDGET OFFICER
BUREAU DU DIRECTEUR PARLEMENTAIRE DU BUDGET

The Parliamentary Budget Officer (PBO) supports Parliament by providing economic and financial analysis for the purposes of raising the quality of parliamentary debate and promoting greater budget transparency and accountability.

The PBO received multiple parliamentary questions regarding contingent liabilities. Specifically, how they are recorded from a financial perspective, and the reason for the increase in recent years. This report provides additional information to answer these questions.

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Highlights

The PBO received multiple parliamentary questions regarding contingent liabilities. Specifically, how they are recorded from a financial perspective, and the reason for the increase in recent years. This report provides additional information to answer these questions.

Summary

This report provides additional information to answer parliamentary questions regarding contingent liabilities. Specifically, how they are recorded from a financial perspective, and the reason for the increase in recent years.

Contingent liabilities can be defined as possible obligations that may result in future payments when one or more future events occur or fail to occur. These events may not wholly be within the control of the government but may arise during the normal course of operations.

When the probability of a future payment is considered likely, and the amount can be estimated, the government records a provision for the contingent liability. The current estimate of outstanding contingent liabilities, as of March 31, 2023, is \$76 billion. Since 2016, the stock of outstanding contingent liabilities has grown, on average, by roughly 30 per cent annually.

A large portion of the increasing provision for contingent liabilities can be attributed to Indigenous claims. As noted in the Public Accounts of Canada 2023, the government recorded expenses totaling approximately \$26 billion related to Indigenous claims in 2022-23. This reflects, as stated by the government, its "efforts to work with Indigenous partners to collaboratively address past injustices and to accelerate the resolution of litigation and the implementation of negotiated settlements to support reconciliation in Canada."¹

Given that expenses related to the provision for contingent liabilities can have a large impact on the federal government's budgetary balance, parliamentarians may wish to:

- Request additional information on how the government estimates these liabilities as part of its fiscal forecast, as well as additional disclosures on potential uncertainty or risk; and,
- Request additional details or disclosures to better track these liabilities across different financial documents.

Overview

The PBO received multiple parliamentary questions regarding contingent liabilities. Specifically, how they are recorded from a financial perspective, and the reason for the increase in recent years. This report provides additional information to answer these questions.

What are contingent liabilities?

Contingent liabilities can be defined as possible obligations that may result in future payments when one or more future events occur or fail to occur. These events may not wholly be within the control of the government but may arise during the normal course of operations.

Examples of contingent liabilities include:

- Loan guarantees;
- Insurance programs;
- Callable share capital in international financial institutions; and,
- Claims and pending and threatened litigation.

This last category includes specific claims that deal with the past grievances of First Nations related to Canada's obligations under historic treaties or the way it managed First Nations' funds or other assets, and comprehensive land claims where Aboriginal rights and title have not been resolved by treaty or by other legal means.²

When the probability of a future payment is considered likely, and the amount can be estimated, the government records a provision for the contingent liability. The Treasury Board Secretariat's Directive on Accounting Standards related to contingent liabilities provides the guidelines outlined in Table 1.

Table 1
Accounting treatment for contingent liabilities

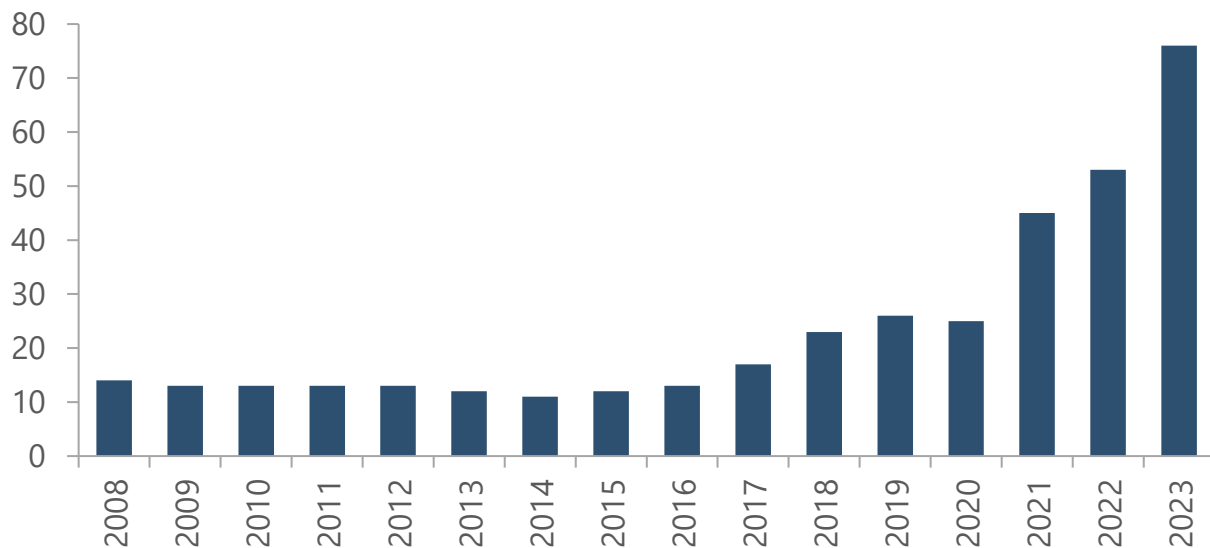
Probability that a liability exists	Likely (> 70%)	Not determinable (30-70%)	Unlikely (< 30%)
Amount can be estimated	Record an estimated liability *	Disclose in notes	Do not disclose in notes or record
Amount cannot be estimated	Disclose in notes	Disclose in notes	Do not disclose in notes or record

Source:
Treasury Board of Canada Secretariat.

Note:
* There are two exceptions to this rule for departmental financial statements. See endnote 3 for more details.³

The current stock of the outstanding provision for contingent liabilities, as of March 31, 2023, is \$76 billion. This amount has increased significantly in recent years, with an average annual growth of roughly 30 per cent since 2016 (Figure 1).

Figure 1
Provision for contingent liabilities (in billions of dollars)



Textual description:

Year	Provision for contingent liabilities (in billions of dollars)
2008	14
2009	13
2010	13
2011	13
2012	13
2013	12
2014	11
2015	12
2016	13
2017	17
2018	23
2019	26
2020	25
2021	45
2022	53
2023	76

Source:

Public Accounts of Canada 2023; Volume 1; Section 1

Note:

The amounts are as of March 31 of each year.

When considering the Government's entire exposure to contingent liabilities, the total increases to over \$2 trillion. However, the majority of this does not meet the criteria of a future payment either being likely to happen or where the amount can be estimated.

How does the Government record these liabilities?

From an accounting perspective, when the probability of a future payment is considered likely, and the amount can be estimated, the Government records a provision for the contingent liability and the amount is expensed in that fiscal year. This amount reduces the budgetary balance and is then reflected in the fiscal framework. The increase in the

provision for contingent liabilities is captured on the Government's balance sheet under accounts payable and accrued liabilities. These contingent liabilities are reviewed on a quarterly basis, and if the value or likelihood of the estimate changes, then they are adjusted at that point in time.

When the uncertainty is removed, and the contingent liability becomes an actual liability, the Government would decrease the provision for contingent liabilities by the final amount. There would be an offsetting increase in other accounts payable and accrued liabilities.

Once the final payment is made, there would be offsetting reductions to liabilities and assets (cash). While this final step affects the cash requirements, it would not impact the budgetary balance as it has already been expensed.

The cash expenditure can occur in a different fiscal year than when it was expensed. An example of this would be the First Nations Child and Family Services program and Jordan's Principle, where the Department of Indigenous Services Canada had budgetary authorities for the settlement in 2023-24, but a large portion of the payment was expensed and recorded by the government as a provision for contingent liabilities in the 2020-21 fiscal year.⁴

What is driving the increase in the provision for contingent liabilities?

As highlighted above, the provision for contingent liabilities significantly increased in recent years. Table 2 demonstrates that the increase can be attributed to claims, which the government groups into three categories:

- Pending and threatened litigation and other claims;
- Specific claims, which deal with the past grievances of First Nations related to Canada's obligations under historic treaties or the way it managed First Nations' funds or other assets; and,
- Comprehensive land claims, which arise in areas of the country where Aboriginal rights and title have not been resolved by treaty or by other legal means.

Table 2

Components of the provision for contingent liabilities (in billions of dollars)

Year	2019-20	2020-21	2021-22	2022-23
Pending and threatened litigation and other claims	6.7	25.6	30.8	42.7
Specific claims	10.8	11.5	15.2	23.6
Comprehensive land claims	6.7	6.9	7.1	9.3
Total claims	24.2	44.1	53.0	75.5
Provision for guarantees provided by the government	0.8	0.7	0.4	0.5
Total provision recorded	24.9	44.8	53.4	76.0

Source:

Public Accounts of Canada.

Note:

The amounts are as of March 31 of each year. Numbers may not add due to rounding.

A large portion of the increasing provision for contingent liabilities can be attributed to Indigenous claims. As noted in the Public Accounts of Canada 2023, the government recorded expenses totaling approximately \$26 billion related to Indigenous claims in 2022-23. This reflects, as stated by the government, its "efforts to work with Indigenous partners to collaboratively address past injustices and to accelerate the resolution of litigation and the implementation of negotiated settlements to support reconciliation in Canada."⁵

Indigenous claims can be grouped into four main categories, as follows:⁶

- Comprehensive land claims, which arise in areas of the country where Aboriginal rights and title have not been resolved by treaty or by other legal means;
- Specific claims, which deal with the past grievances of First Nations related to Canada's obligations under historic treaties or the way it managed First Nations' funds or other assets;
- General litigation claims being pursued through the courts, which include compensation related to the First Nations Child and Family Services program, Jordan's Principle, and residential schools; and,

- Special claims, which represent claims that are not being pursued through the courts and that do not fit within the parameters of existing policies for Comprehensive Land Claims or Specific Claims.

Given the large expense in 2022-23, and the recent increase in the provision for contingent liabilities, the PBO sent information requests to both Indigenous Services Canada (ISC) and Crown-Indigenous Relations and Northern Affairs Canada (CIRNAC) seeking the amount of expenses recorded by the government related to Indigenous claims over the last three fiscal years (2020-21 to 2022-23).⁷ The information provided showed that the main factor behind the increase in Indigenous claims results from revaluations of existing claims (Table 3) rather than new claims that can be estimated and are considered likely.

Table 3

Expenses for Indigenous claims (in billions of dollars)

Year	2020-21*	2021-22	2022-23
New claims – ISC	1.9	6.4	0.0
Revaluation of existing claims - ISC	0.0	-2.1	3.3
Total expenses - ISC	2.0	4.3	3.3
New claims – CIRNAC	1.5	4.4	3.8
Revaluation of existing claims - CIRNAC	4.7	4.6	18.9
Total expenses - CIRNAC	6.2	9.0	22.7
New claims – Total	3.4	10.8	3.8
Revaluation of existing claims - Total	4.7	2.5	22.2
Total expenses	8.1	13.3	26.0

Source:

Indigenous Services Canada (IR0713) and Crown-Indigenous Relations and Northern Affairs Canada (IR0714).

Note:

* The 2020-21 amounts do not include the expenses accrued for the First Nations Child and Family Services program and Jordan's Principle, as this was centrally booked by the Office of the Comptroller General, and subsequently transferred to ISC in 2021-22. However, since these amounts were accrued in prior fiscal years, there was no impact on expenses in 2021-22. This is in line with the Directive on Accounting Standards: GC 3300-3310 Contingent Liabilities and Loan Guarantees. See endnote 3 for more detail on these accounting standards.

New claims refer to when they first meet the criteria of being considered likely and can be estimated.

Numbers may not add due to rounding.

Considerations for parliamentarians

As shown in recent years, expenses related to the provision for contingent liabilities can have a large impact on the federal government's budgetary balance. While the Public Sector Accounting Standards require that contingent liability estimates be recorded for claims only when there is a high degree of likelihood of a liability and when the amount of the claim is estimable, the final amounts can significantly vary from the original estimate.

This is especially the case for claims proceeding through the courts and alternative dispute resolution mechanisms, as the estimate may change as new information becomes available. Parliamentarians may wish to seek additional information on how the government estimates these potential liabilities as part of their fiscal forecast. They may also wish to seek additional disclosures on potential uncertainty or risk to the budgetary balance beyond the liabilities already booked, for example on additional potential liabilities being monitored by departments.

It is also difficult to track contingent liabilities between the different publicly available financial documents, notably from the initial point a provision is accrued until it is paid out. For example, when a department is requesting new authorities for a claim in an Estimates document, it can at best be challenging, and often nearly impossible, to understand whether the provision has already been accrued and expensed and in which year. Parliamentarians may wish to seek additional details or disclosures to better track these liabilities across the different financial documents.

Notes

¹ [Public Accounts of Canada 2023](#); Volume 1; Section 1.

² [Public Accounts of Canada 2023](#); Volume 1; Section 2.

³ For departmental financial statements, the following two exceptions apply. Specifically, when the magnitude of the estimated liability is so significant that its inclusion in expense/liabilities would risk revealing the estimate of the potential liability, or if the contingency relates to decisions of TBS as the public service employer and the potential impact of the claim extends across many departments. If these situations arise, the departments must consult with the Office of the Comptroller General of Canada (OCG) to determine how it will be disclosed.

Further information can be found in the [Directive on Accounting Standards: GC 3300-3310 Contingent Liabilities and Loan Guarantees](#).

⁴ [Public Accounts of Canada 2021](#); Volume 1; Section 2.

⁵ [Public Accounts of Canada 2023](#); Volume 1; Section 1.

⁶ [Public Accounts of Canada 2023](#); Volume 1; Section 1.

⁷ [IR0713](#) and [IR0714](#).

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