

17.**REVIEW OF FINANCIAL STATEMENTS AND
MANAGEMENT LETTERS****INTRODUCTION**

17.1 The financial statements of crown corporations and agencies of the government of Nova Scotia are in some cases audited by the Office of the Auditor General and in other cases by private sector auditors. A complete list of crown corporations and agencies that have been audited is included in Appendix II.

17.2 Section 17 of the Auditor General Act permits this Office to conduct additional reviews of crown corporations and agencies audited by the private sector. This section of our Report contains comments on financial statement audits conducted by the private sector and by this Office.

AUDITS BY THE PRIVATE SECTOR

17.3 We reviewed the financial statements audited and management letters prepared by private sector auditors, being principally interested in whether:

- there was any indication of inadequate controls or accounting records;
- there was timely preparation and audit of annual financial statements;
- there were notes to the financial statements outlining the legislative mandate of the entity; and
- there was adequate public disclosure of the entity's audited financial statements, preferably in the *Public Accounts*.

17.4 The following are the observations resulting from our review.

Reservations of Opinion

17.5 A qualification of opinion was expressed in the audited financial statements of two corporations.

17.6 *Highway 104 Western Alignment Corporation* - The auditors issued a qualification of opinion due to deficiencies in the Corporation's tolling system. For the four-month period ended March 31, 1998, the auditors were unable to obtain sufficient evidence with respect to the completeness of operating revenue and the accuracy of customer account balances.

17.7 *Nova Scotia Resources Limited* - The auditors issued a qualification of opinion due to the failure of the Corporation to defer and amortize foreign exchange gains and losses on long-term monetary items over the term of the related debt. If they had been deferred and amortized, the net loss would have increased by \$3.4 million, the opening deficit would have been reduced by \$3.4 million, and unamortized foreign exchange losses carried forward would be nil.

Financial Controls and Records

17.8 As a result of the private sector audits, weaknesses in internal control were discovered in certain corporations and agencies, and were described in letters from the auditors to management. Many of these are not serious enough to include in this Report. However, some observations were more significant, and are summarized below.

- The auditors of Highway 104 Western Alignment Corporation noted they encountered numerous deficiencies in the highway operator's tolling system and control procedures. They recommended that the Corporation undertake a regular review of the operator's systems and controls to ensure they are adequate and adhered to on a regular basis. The auditors also recommended the establishment of a process for monitoring the funding and distributions for each of the Corporation's reserve accounts.
- The auditors of the Nova Scotia Alcohol & Gaming Authority reported weaknesses in control over cash receipts and the processing of journal vouchers. The auditors also recommended the Authority take steps to ensure computers and systems are Year 2000 compliant.
- The auditors of the Nova Scotia Arts Council noted that accounting policies and procedures require substantial improvement. Weaknesses were identified in control over cash receipts and official donation slips, payroll records and procedures, bank and general ledger reconciliation procedures, and the process of paying supplier invoices.
- The auditors of the Nova Scotia Liquor Commission noted that accounts receivable and payable subledger reconciliation procedures were not being completed. Last year the auditors reported the need for clarification of responsibilities in the Memorandum of Understanding between the Department of the Environment and the Commission, concerning which organization is to absorb the net gain or loss of the Commission's bottle return program. The auditors noted there was no resolution of this issue during the year.
- The auditors of the Resource Recovery Fund Board Inc. noted a need for regular monitoring of perpetual inventory records and the performance of periodic inventory counts.
- The auditors of the Sherbrooke Restoration Commission reported weaknesses in control over inventory and in bank reconciliation procedures. In addition, the auditors recommended that the Commission investigate the source of computer system problems identified by management and staff, and take steps to ensure computers and systems are Year 2000 compliant.
- The auditors of the Waterfront Development Corporation Limited noted a lack of adequate reconciliation of Harmonized Sales Tax (HST) remittances with the general ledger's HST accounts.

Timeliness of Financial Reporting and Release of Management Letters

17.9 We believe the preparation, audit and release of financial statements and related management letters within six months of year-end is satisfactory.

17.10 The audited financial statements for Sydney Steel Corporation had not been approved and released by the time of the writing of this Report, approximately ten months after year-end. Draft unapproved financial statements for the year ended December 31, 1997 are to be included in the March 31, 1998 *Public Accounts*. Last year we reported that the audits for the 1995 and 1996 fiscal years for Sydney Steel Corporation were not completed. Neither of these two audits were finalized during the current year.

Legislative Mandate

17.11 It is important for the reader of financial statements to be aware of the legislative mandate under which the entity operates. This is most conveniently communicated as a note to the financial statements, but can also be described in an entity's annual report. It is recommended that all crown corporations and agencies include such a note in their financial statements.

17.12 All crown corporations and agencies included in our review complied with this recommendation.

Reporting

17.13 Previous Reports of the Auditor General have recommended that the *Public Accounts* present audited information on the financial position and operating results of all entities which are owned or controlled by government.

17.14 The March 31, 1998 *Public Accounts* do not contain the annual financial statements of the following government-controlled entities.

- Halifax-Dartmouth Bridge Commission
- Nova Scotia Credit Union Deposit Insurance Corporation
- Workers' Compensation Board of Nova Scotia

17.15 In addition, the financial statements of joint operations with other governments are not included in the *Public Accounts*. These include the Atlantic Lottery Corporation Inc., Canada-Nova Scotia Offshore Petroleum Board and the Council of Maritime Premiers.

AUDITS BY OFFICE OF THE AUDITOR GENERAL

17.16 The following observations resulted from financial statement audits conducted by the Office of the Auditor General of Nova Scotia.

Reservations of Opinion

17.17 This Office has responsibility for the annual financial statement audit of 25 crown corporations and agencies (Appendix II). An audit opinion is expressed on whether these statements present fairly the financial position of the entity at its fiscal year-end and the results of its operations for the year then ended. Where there are qualifications of audit opinion, or situations in which it was not possible to render an opinion, we believe it appropriate to report such to the House of Assembly.

17.18 The Auditor's Reports on the March 31, 1998 financial statements of the Nova Scotia Business Development Corporation Fund and the Industrial Expansion Fund were qualified due to the fact that Executive Council approval of write-offs being reported, required under Section 23 of the Provincial Finance Act, was still outstanding when the statements were released.

System Weaknesses

17.19 We noted situations during our audits where accounting and control systems and procedures were deficient. Although they were not of a magnitude to require reservations of audit opinion, a number of these situations are significant enough to include in this Report.

17.20 *Insured Prescription Drug Plan Trust Fund (Seniors' Pharmacare)* - The Seniors' Pharmacare program has incurred deficits totalling \$23.0 million for the three years ended March 31, 1998; due primarily to revenues being insufficient to meet program costs. The Department of Health has funded the deficits to date. Various options for eliminating continuing revenue shortfalls have been examined by the Seniors' Pharmacare Board and the Department of Health. However, no decision has been made concerning program changes to prevent future revenue shortfalls and ensure the program is sustainable over the longer term.

17.21 *Nova Scotia Business Development Corporation* - We noted a lack of segregation of duties relating to the receiving and recording of funds. Compensating controls have been put in place to address this control weakness, but further improvements are required. Staff have indicated that they have addressed this situation in the current year.

17.22 *Nova Scotia Farm Loan Board* - We noted that total loan advances and repayments, as well as other account balances recorded in the Board's financial records, did not agree to the amounts recorded in the Province's accounting records maintained by the Department of Finance. A reconciliation of the Board's records with those at the Department of Finance was not performed until year-end; and upon completion no explanation could be provided for the differences. We recommended that monthly reconciliations be performed on a timely basis.

17.23 *Nova Scotia Fisheries and Aquaculture Development Fund* - The Board of the Fisheries and Aquaculture Development Fund is comprised of ten members from various areas of the Province, all of whom are appointed by Executive Council. At the time of our audit, one Board member was also a senior employee of a company which was the single largest borrower from the Fund. We noted from a review of Board minutes that the member abstained from votes concerning his company's loan applications, but did participate in related discussions. We understand that no other loan applicant has a similar opportunity to appear before the Board to present a case for financial support. We also noted that the Board member participated in discussions concerning loans and guarantee applications of competitors to his company. Upon follow-up, a few months after our audit, we were informed that this person is no longer a member of the Board of Directors.

17.24 *Nova Scotia Housing Development Corporation* - In 1997, the Corporation entered into an agreement to transfer the administration of certain social housing programs from Canada Mortgage and Housing Corporation (CMHC) to the Corporation. In our testing of transactions we noted that legal documents to support the existence, ownership and cost-sharing arrangements for various social housing assets were missing from program files.

17.25 *Provincial Drug Distribution Program* - The Provincial Drug Distribution Program supplies drugs to health care facilities in the Province and is administered by the Nova Scotia Hospital. The Program contracts with vendors in the private sector to supply drugs. The Program may purchase pharmaceuticals from an alternate source if the contract vendor is unable to deliver the items as specified in the contract. Under terms of the contract, the difference between the contract price and the alternate supply price may be recovered from the contract vendor. Currently, the amounts are not recovered and are borne by the Program. We recommended that staff recover from contract vendors all amounts to which the program is entitled. Program management has indicated that the recommendation will be implemented.

17.26 Public Trustee Trust Funds - We noted control weaknesses in the cash receipt and disbursement systems. We recommended that the mail book be reconciled to bank deposits on a regular and timely basis and forms for recording receipts and disbursements be prenumbered.

Legislative and Policy Compliance Weaknesses

17.27 We noted situations where there was lack of compliance with legislation or policy. Although they were not of a nature to require a reservation of audit opinion, four of these situations are significant enough to describe in this Report.

17.28 Nova Scotia Business Development Corporation - We observed that the Finance Committee, a committee of the Board of Directors, had not reviewed the reserves, arrears and write-offs of the Corporation prior to the preparation of the draft financial statements. In order to comply with the terms of reference approved for the Committee and to improve controls over the management of the funds, the write-offs, reserves and arrears should be reviewed by the Finance Committee prior to finalization of the draft financial statements.

17.29 Nova Scotia Hospital - The Corporate Services Committee of the Hospital approved the writing off of bad debts of \$278,000. Executive Council approval for the write-offs was not sought, as had been done in previous years. Hospital staff obtained an opinion from Department of Finance staff which led them to believe this approval was not required. We recommended that the Hospital seek a legal opinion with respect to whether the requirement for Executive Council approval for write-offs, as described in Section 23(1) of the Provincial Finance Act, applies to the Hospital.

17.30 As we reported in previous years, Section 30 of the Hospitals Act stipulates that, 30 days after receiving a written notice of discharge, a patient is solely liable for his or her costs of maintenance as long as the individual continues to stay in a hospital. The Hospital Board of Management decided not to issue invoices or 30-day notices to these patients because the vast majority were deemed to be financially incapable of paying these costs. The practice was continued this year with the approval of the Department of Health. This practice also contravenes Section 23 (1) of the Provincial Finance Act which requires the Executive Council to approve write-offs or settlements of Provincial claims against a person.

17.31 Pension Funds - The Teachers' Pension Act requires that a formal actuarial valuation be conducted for the Teachers' Pension Fund every three years. The Fund was due for its triennial valuation effective July 31, 1997. However, the valuation was not started until the latter part of 1998 and had just been finalized at the time this Report went to print in December 1998. At the request of management, we deferred the completion of our audit of the Fund's March 31, 1998 financial statements until this valuation was completed.

17.32 Originally, it was thought that the Public Service Superannuation Fund (PSSF) was due for its triennial actuarial valuation as at March 31, 1998 since the Fund's March 31, 1997 statements indicated the last such review was completed as at March 31, 1995. However, it was subsequently brought to our attention that a full valuation had been completed as at December 31, 1996. We were not provided timely notice of this review and, as a consequence, there was a significant delay in the completion of our audit of the PSSF's March 31, 1998 financial statements.

17.33 The Teachers' Pension Act provides for the appointment of a Teachers' Pension Board. However, after passing of the new Act in 1989 the terms of Board members were allowed to expire, with no effort made to appoint new members. As a result, the Board ceased to function for a period. Board appointments were made effective May 1998. However, management indicated that, pending planned changes to the Act, the current appointments were made to deal with appeals only, and not all of the other Board responsibilities under the Act.

17.34 Changes to the Members' Retiring Allowance Act on November 25, 1993 established the Members' Supplementary Retiring Allowances Plan. As in prior years, we recommended that there be an appropriate segregation of the accounting for and reporting on the supplementary plan's contributions, interest, refunds and allowances from that of the original plan.

17.35 *Upper Clements Family Theme Park Limited* - Upper Clements Family Theme Park Limited entered into an agreement with a private sector agency for the operation of the Park. We noted that the crown corporation may not have fully complied with the agreement with respect to the timing of the payment of annual operating grants.

Financial Statement Audit Delays

17.36 We consider readiness of the auditee to be a critical factor in the timely completion of financial statement audits.

17.37 The Auditor's Report for the Nova Scotia Teachers' Pension Fund's March 31, 1998 financial statements had not been issued at the time of writing this Report because management had been waiting for completion of the actuarial valuation necessary for the completion of the financial statements.
