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REVIEW OF FINANCIAL STATEMENTS AND MANAGEMENT LETTERS

INTRODUCTION

- 8.1** The financial statements of crown corporations and agencies, funds of the government of Nova Scotia, and trusts administered by 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 licensed under the Public Accountants Act.
- 8.2** Section 17 of the Auditor General Act permits this Office to conduct additional reviews of those entities where financial statements are reported on by private sector auditors. This Chapter contains comments on our review of the results of financial statement audits by private sector auditors, as well as comments on audits performed by this Office.

FINANCIAL STATEMENT AUDITS

- 8.3** The Auditor General is responsible for the annual audit of the consolidated financial statements of the Province of Nova Scotia. See Chapter 2 of this Report for comments and observations on our audit of the Province's March 31, 2006 statements.
- 8.4** In preparing this chapter, we reviewed the audited financial statements and reports prepared by our Office and by private sector auditors. Our review focused on whether:
- there were any qualifications of auditors' opinions on the financial statements;
 - the audit opinion was based on Canadian generally accepted accounting principles, or on a disclosed basis of accounting;
 - there was any indication of inadequate controls over accounting records; and
 - there was timely preparation and audit of annual financial statements.
- 8.5** The following observations resulted from our review.

Reservations of Opinion

- 8.6** The result of an audit is an opinion on whether financial 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 an audit opinion or situations in which it was not possible to render an opinion, we believe it is appropriate to report on such matters and have done so below.

8.7 Qualified audit opinions were issued by the auditors of:

- *Halifax Regional School Board, South Shore Regional School Board, Strait Regional School Board, Tri-County Regional School Board, Annapolis Valley Regional School Board, and Conseil scolaire acadien provincial* due to concerns about the controls over school-based funds.
- *Art Gallery of Nova Scotia* due to insufficient evidence to indicate whether revenue is complete, which is consistent with prior years.
- *E911 Cost Recovery Fund* due to insufficient evidence to indicate whether expenses of the fund are complete.
- *N.S. Farm Loan Board* because of insufficient, satisfactory evidence relating to management's estimate of provisions for loan and real estate impairment.
- *Public Trustee* due to insufficient evidence to indicate whether trust income and assets are complete, which is consistent with the prior year.
- *Cumberland Regional Economic Development Association* due to the valuation of long-term investments.

Disclosed Basis of Accounting

8.8 As the result of changes to the Canadian Institute of Chartered Accountants Handbook, auditors can no longer give unqualified opinions on general purpose financial statements unless the statements comply with Canadian generally accepted accounting principles (GAAP). Audit reports on financial statements prepared using a disclosed basis of accounting, rather than GAAP, are deemed to be for specific users - not for general purpose - and should include wording similar to the following:

“these financial statements, which have not been, and were not intended to be, prepared in accordance with Canadian generally accepted accounting principles, are solely for the information and use of (the addressee) and; the regulator or legislator ... for the (purposes(s)), and are not intended to be and should not be used by anyone other than the specified users, or for any other purpose...”

8.9 The preparation of financial statements on other than a GAAP basis reduces the value of the statements to the House and the general public.

8.10 The following entities' financial statements were prepared on a disclosed basis of accounting rather than Canadian generally accepted accounting principles.

- *N.S. Power Finance Corporation* - The financial statements were prepared on a disclosed basis of accounting.

- *Sherbrooke Restoration Commission* - The financial statements were prepared using accounting principles for museum boards in Nova Scotia as prescribed by the Department of Tourism, Culture and Heritage.

Financial Controls and Records

8.11 During financial statement audits, situations were noted where accounting and control systems or procedures were deficient. These weaknesses in internal controls were reported by the auditors in management letters to the crown corporations or agencies. Although they were not of a magnitude to require reservation of an audit opinion, the more significant observations are summarized below under each entity's name.

Regional School Boards

- *Annapolis Valley Regional School Board* - All advances to individuals should be reconciled to the receipts and money returned.
- *Chignecto-Central Regional School Board* - Collection of fees from a particular organization was slow. The auditors noted that since payment is not expected within the next year, classification of the liability as current might not be in accordance with GAAP. The auditors were also concerned about collectability of the balance.
- *South Shore Regional School Board and Tri-County Regional School Board* - There was no formal process for documenting, testing and evaluating internal controls at the Boards. There was also no formal process to identify and evaluate internal and external business risks. Approval and documentation for electronic cheque signatures were not necessarily sufficient, although both signatures appeared on the cheques as required. The Information Technology function does not have explicit plans and objectives that are aligned with the Boards plans and objectives. Also system event logs and activity reports for the server at the Finance Department are not being reviewed and evaluated, and no security policies and procedures are in place for setup of new users or termination of existing users.
- *South Shore, Tri-County, Halifax, and Strait Regional School Boards* - A CICA Section 5900 Auditor's Report on the SAP Customer Competency Center reported that there were internal control exceptions identified in the operating effectiveness of a number of internal control procedures that support the overall control objectives. Management needs to assess the risks these exceptions have on their individual financial reporting environments.
- *Strait Regional School Board* - Bank reconciliations were not done consistently for school-generated fund activities. Also, cheques were presigned with one signature and not kept in a secure location. There was no regular backup up of financial information.

- *Halifax Regional School Board* - Cash is not always accompanied by the correct forms and receipts are not consistently issued for funds received. The 68% refund of HST is not claimed on a consistent basis. Not all cheques had two signatures, and some cheques had the payee as one of the signatures. Also, not all schools received cancelled cheques from the bank and there is no formal process for approving all invoices.

District Health Authorities

- *Annapolis Valley District Health Authority, South West Nova District Health Authority and South Shore District Health Authority* - A number of receivable balances had been outstanding for extended periods of time. Funding from Foundations and Auxiliaries relating to their commitments is not being invoiced in a timely manner. Also, there was no formal, documented Disaster Recovery Plan for recovery of the information processing environment. Information Services is not notified of employee departures in some districts. Test results are not retained for changes to applications, the network and the operating systems. There was a need to improve the timeliness of financial reporting and the turnaround of variance analysis. In addition, the auditor for Annapolis Valley District Health Authority noted gaps in processes surrounding the control of certain “controlled substances”.
- *Cape Breton District Health Authority* - Several employees have vacation carried forward from prior years in excess of amounts permitted in the Authority’s policies. Expenditures for one supplier were broken down into three invoices so each invoice would be under an employee’s authorization threshold. Also, there is a lack of review of wage entitlement status which could result in inaccurate payments to employees.
- *Colchester East Hants Health Authority* - Revenues, receipt of payments, and recording duties were not properly segregated. Additionally, payroll functions were not appropriately segregated.
- *Cumberland Health Authority* - The accounts receivable subledgers were not reviewed in sufficient detail prior to the audit and receipts were not posted in the proper periods, resulting in audit adjustments. The materials management accrual report was not accurate and accruals at month end had been consistently understated by an unknown amount. Also, employee payroll files are kept in boxes in the common area of the Finance Department with no restricted access. Various employees have access rights to the financial system that are inappropriate.
- *Guysborough Antigonish Strait Health Authority* - Several packing slips or invoice audit blocks were not initialled as evidence of receipt of the goods or services. Also, certain time cards were not appropriately approved.
- *Pictou County Health Authority* - Certain journal entries were not appropriately reviewed and/or approved by management. Some senior management have

access to both accounts payable and payroll master files. Also, all payroll clerks can access and change employee master files.

Other Entities

- *Insured Prescription Drug Plan Trust Fund* - Certain business users have administrator access rights to financial applications. Also, security events occurring at both the operating system and database level are not reviewed.
- *Izaak Walton Killam Health Centre* - Certain users are allowed to emulate other users, that is access the system with all the rights of the other users. Such usage is tracked in a log that is not being regularly reviewed. The emulation rights should be removed or the log reviewed on a regular basis. Also regular reviews of users' access to key applications was not being performed.
- *Nova Scotia Business Inc.* - Payroll input to SAP was not compared to supporting documents. Segregation of duties in the payroll process was not appropriate. Also, there was no independent management review or approval of SAP journal entries and the support for the journal entries was not consistently maintained. No procedures were in place to ensure that all data entered into the loan portfolio management system was reviewed and approved. Year end valuation for the annual loan review process was not always based on the most current, third-party information.
- *Nova Scotia Farm Loan Board* - Inadequate monitoring of loans, lack of documentation to support the loan valuation process, and weaknesses in business processes and internal controls resulted in the inability to conclude on the accuracy of provisions for real estate impairment.
- *Nova Scotia Fisheries and Aquaculture Loan Board* - The Board's books of accounts do not report all transactions and the balances of these accounts do not equal the amounts in the financial statements. The loans subledger and general ledger are not reconciled. There is inadequate documentation supporting the allowance amount for impaired loans. Vessel inspections, which are the basis for the allowance for impaired loans, are not being done as frequently as the Board's policy requires. Also, interest accrued prior to declaring a loan to be impaired was not being included in the allowance for loan impairments.
- *Nova Scotia Gaming Foundation* - The amount of any surplus that is to be transferred to the Community Development Account (CDA) is not clearly outlined in the Memorandum of Agreement (MOA) and should be agreed upon by the N.S. Gaming Foundation and the Department of Health Promotion and Protection. Also, the Foundation is not complying with one section of the MOA which requires the Department of Finance to invest the CDA balance. This section of the MOA should be reviewed and amended if appropriate.
- *Nova Scotia Health Research Foundation* - There were problems with the accuracy and completeness of the accounts and grants payable systems which have been

an ongoing concern since the auditor's involvement with the Foundation. The Foundation's investment policy has a primary objective of preservation of capital; however, the Foundation is now investing in equity mutual funds, including significant foreign holdings. These investments suggest an objective of maximizing returns which is contrary to the investment policy. The current portfolio could have a negative impact on the Foundation's financial position if there was a significant downturn in the equity market.

- [Nova Scotia Legal Aid Commission](#) - The accounts payable subledger is out of balance with the general ledger again this year. Payments to the Board of Directors did not have corresponding T4s or T4As issued.
- [Nova Scotia School Boards Association](#) - The non-teachers pension plan is not being audited, contrary to the declaration of Trust of the plan.
- [Agritech](#) - Agritech uses the tangible capital assets policy of the Province. Due to the size of Agritech, that is not appropriate. Items that are material to Agritech fall below the Province's thresholds for capitalization and are being expensed. Also, Agritech does not have an inventory of capital assets.
- [Members' Retiring Allowances Act Accounts](#) - The interest rate used by the actuary in his evaluation differs from that prescribed by regulation to be applied to the accounts. The actuary reported required additional contributions higher than those prescribed by negotiations. The Members' Retiring Allowance Act Accounts are an unfunded pension obligation and this is not clear in the Financial Statements or the Actuarial Valuation.
- [Resource Recovery Fund Board](#) - One approved program had been withdrawn but the amount approved was still recorded as committed. Some funding files were missing the approved program funding payment sheet. Also, one file had a final payment notice, but still had an amount outstanding.
- [Sherbrooke Restoration Commission](#) - Management does not document evidence of review of monthly bank reconciliations and a number of blank cheques had been presigned.
- [Canada-Nova Scotia Offshore Petroleum Board](#) - The Board should consider forming a separate audit committee to review financial statements, etc.
- [N.S. Long Term Disability Plan](#) - Premiums and Employment Insurance rebates received are not verified for accuracy.
- [Highway 104 Western Alignment Corporation](#) - Concern was expressed about electronic systems security.
- [N.S. Liquor Commission](#) - Management should implement a more robust capital asset project accounting and approval process and certain Balance Sheet accounts, though not materially misstated, require reconciliation.

Timeliness of Financial Reporting

- 8.12** The Provincial Finance Act requires that financial statements for government business enterprises and governmental units be submitted to the Minister of Finance by June 30 following the fiscal year end (usually March 31).
- 8.13** There continue to be problems with receiving submissions by the deadline. This year, there were 20 entities (21 in 2005) that were not successful in providing audited financial statements and requested information by June 30.
- 8.14** The Province's March 31, 2006 consolidated financial statements were released on September 29, 2006 meeting the reporting requirement set out in the Provincial Finance Act.
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