REPORT OF THE

AUDITOR GENERAL

1997

Honourable Gerald G. Fogarty
Speaker
House of Assembly

Sir:

I have the honour to submit herewith my Report to the House of Assembly for the year ended March 31, 1997, to be laid before the House in accordance with Section 9(2) of the Auditor General Act.

Respectfully submitted

[original signed by E. R. Salmon]

E. Roy Salmon, F.C.A.
Auditor General

Halifax, Nova Scotia
January 12, 1998

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1.

OVERVIEW AND SIGNIFICANT ISSUES

INTRODUCTION

1.1 This Report contains the results of work carried out by my Office during 1997. My objective is to provide information to the House of Assembly to aid its members in carrying out their responsibility to hold the government to account for the management of public funds.

1.2 In performing our work we adhere to the standards promulgated by the Canadian Institute of Chartered Accountants (CICA). New standards for assurance engagements were issued in March 1997 by the CICA. We are currently reviewing our audit processes and reporting style to ensure that we fully comply with them.

1.3 This chapter provides a summary of the most significant findings outlined in the Report. The individual chapters provide the more detailed results of each audit or review and contain other issues which require attention. In addition, during 1997 I issued a Special Report dealing with the Province's financial statements for the year ended March 31, 1997. I caution readers of this chapter that a fuller understanding of any particular issue would be obtained from reading the more detailed chapter or report.

1.4 Within government, efforts continued to improve management processes and accountability reporting. Some of these respond to recommendations and observations made in previous Reports. This Report comments on these initiatives and provides status reports. Many of these initiatives are positive, but our work also identified significant issues which warrant action.

AUDIT MANDATE

1.5 The Auditor General Act requires me to table this *Report of the Auditor General* on a day following the day that the government tables the *Public Accounts*. These have generally not been tabled until March of the year following the end of the previous fiscal year. However, in the spring of 1997 an amendment to the Provincial Finance Act was passed, requiring the *Public Accounts* to be tabled or deemed tabled by December 31 following the end of the fiscal year. This is a positive change, resulting in more timely reporting and will permit more timely release of my Annual Report. Thus, this was a year of transition for my Office and this Report is based on nine months of audit effort. In future years we will endeavor to table the Report very shortly after the Public Accounts are tabled.

1.6 It is also my intention to issue Special Reports when I believe that important information resulting from an audit or review should be provided in a timely manner.

1.7 As has been discussed in previous Reports, and in meetings of the Public Accounts Committee, the Provincial Finance Act provides for an audit of the Province's financial statements by a chartered accountant who reports to the Minister of Finance. This is inconsistent with the traditional view that the Legislature should be the client for this audit, since the Minister is accountable to it for the Province's financial affairs.

1.8 To compensate, at least partly, for this situation, I will continue to review the financial statements and provide commentary on them. This year, because I felt timely information on significant matters was warranted, I issued a Special Report on August 22, 1997 shortly after the financial statements were released. Chapter 2 provides additional comments on these matters.

ACCOUNTABILITY INFORMATION AND REPORTING

1.9 Nova Scotia has received recognition nationally and internationally for its efforts to improve the quality of its accountability information and reporting, particularly its *Government By Design* publication. The government is preparing a performance report entitled *Nova Scotia Counts* that is intended to provide information on the degree to which objectives specified in *Government By Design* were achieved. These are positive initiatives, however they are discretionary. I strongly urge that the provision of such planning information and performance reporting be enshrined in legislation, and that these become key elements of government's accountability relationship with the Legislature.

1.10 Over the past several years the government has made progress in improving the basis of presentation of its financial position and results. However, issues still remain, including the need for full reporting by way of presentation of consolidated statements as a major financial accountability document. In addition, the application of what in my opinion was an inappropriate accounting policy led me to issue a Special Report on the March 31,1997 financial statements.

PROCUREMENT - FOLLOW-UP

1.11 The Procurement Branch of the Department of Finance continues to take significant steps to improve controls over the procurement process. The Branch has taken action on all the opportunities for improvements identified in our Report last year. The implementation of formal reporting on procurement activities and exceptions is to be in place by March 31, 1998.

1.12 Steps have been taken to address the need for a strategy and guidelines for managing P3 within government. However, at the time of our review, further steps were required.

INFORMATION TECHNOLOGY MANAGEMENT - YEAR 2000 READINESS

1.13 The Year 2000 issue has received widespread media coverage and expert commentary. It represents a very real threat to industry and government. If computerized systems are not able to deal with the turn of the century, there may not be the ability to deliver complete and uninterrupted service.

1.14 The government is to be commended for the many steps that have already been taken or are planned. However, there is still much to be done and no one should forget that the deadline is fixed; delay cannot be tolerated.

1.15 I strongly urge the House of Assembly to request periodic reporting on the progress that is being made and the issues that are outstanding.

PUBLIC-PRIVATE PARTNERSHIPS (P3 OR PPP) FOR SCHOOL CONSTRUCTION

1.16 "PPP" is a term that is being used widely, and within government has become a subject of much debate in Nova Scotia, and indeed in other jurisdictions. We examined the government's initial activities in implementing such arrangements for school construction. Our audit identified major deficiencies in the initial processes of analysis, negotiation and agreement finalization.

Similar findings were also reached by a review performed by the Priorities and Planning Secretariat released on December 11, 1997.

1.17 Also in December 1997, the government released a plan for school construction which contemplates the use of public-private partnering arrangements. My Office has not reviewed this plan in detail or reconciled planned funding with the construction timetable. It should be recognized, however, that contemplated leasing arrangements will quickly commit the Province to significant annual expenditures over the next 20 to 25 years. Also the Province will not own the schools when the leases expire. Flexibility in future years may be severely restricted.

1.18 As well, because lease agreements and other arrangements have not been finalized for any of the schools completed or planned, we have not been able to assess the applicability of CICA guidelines for operating leases. These guidelines determine the appropriate accounting treatment. We have also not yet been able to determine whether these arrangements constitute due regard for economy and efficiency, again because agreements have not been finalized.

DEPARTMENT OF FINANCE - CORPORATE FINANCIAL MANAGEMENT SYSTEM (CFMS)

1.19 Implementation of CFMS represented one of the most significant information technology projects undertaken by the government. This Office was concerned about its impact on government and in particular on financial control. However, the review we commenced could not proceed as relevant information could not be obtained on a timely basis. We recognize that this was due to the many priorities being addressed by staff of the Department of Finance and the loss of key staff involved in the project.

1.20 Agreement has been reached with Finance to undertake a joint audit to be completed around March 31,1998. The results of that audit will be released shortly after that date.

DEPARTMENT OF FINANCE - DEBT MANAGEMENT

1.21 There is general agreement that the size of the Province's debt is a matter of some concern. My Office undertook an audit of debt management practices in 1994 and we have continued to monitor Finance's progress in dealing with identified issues.

1.22 My 1995 Report commented positively on actions taken but raised continuing concerns particularly related to the adequacy of resources allocated to this significant financial area.

1.23 This year's review identified continuing action to improve policies and processes and also identified that additional skilled resources had finally been acquired. My Office will continue to monitor the management of the Province's debt in view of its significance to fiscal performance.

ATLANTIC LOTTERY CORPORATION

1.24 An audit conducted by my Office in 1996 identified a number of opportunities to improve the management and governance of ALC. Action has been taken or is underway to deal with many of our recommendations. However, those which require agreement of the four shareholder provinces remain outstanding.

1.25 In particular, a revision to the formula for cost allocation which impacts on profit sharing between the provinces is still under negotiation. In this regard, ALC was using an allocation methodology that was agreed to by the shareholders in 1991. In last year's Report we observed that the manner in which ALC's costs and profit are being allocated using that methodology results in certain shareholder provinces, in essence, subsidizing other jurisdictions. Using information for the 1995-96 fiscal year, we estimated that Nova Scotia was losing approximately $5 million per year.

QUEEN ELIZABETH II HEALTH SCIENCES CENTRE

1.26 I did not conduct an audit of the QE II but do have the mandate to review the results of any audit performed by its auditors. The management letter, issued by its auditors on July 29, 1997, contained issues that warrant attention.

1.27 The concerns relate to the financial position of the Centre because of its accumulated deficit and anticipated future deficits. As at March 31, 1997 the accumulated deficit was $21.9 million and recent public statements indicate a significant deficit in 1997-98. The Centre plans to recover these deficits through future cost savings but also anticipates investing $8.4 million in re-engineering initiatives in order to achieve the savings.

1.28 In addition, certain significant claims and accounts receivable from the Department of Health and the Workers' Compensation Board appear to be under negotiation or in dispute. Any portion uncollected will increase the Centre's deficit.

1.29 In summary, if the Centre is unable to achieve the planned cost savings or the disputed outstanding claims are not recovered, the Province and Centre will have to determine how to finance the resulting large deficit. This could have a significant impact on the Province's goal of balanced budgets.

RESOURCE RECOVERY FUND BOARD INCORPORATED

1.30 This audit resulted in a number of positive findings. However, the manner in which the Board was established raises questions as to its status; is it a government entity or a private concern? It administers a government program, manages public funds and is accountable to a Minister. However, because it is incorporated as a private not-for-profit company, it must pay the Harmonized Sales Tax thus significantly reducing funds available to carry out its programs.

1.31 Another issue is whether it is expected to comply with various government policies including procurement, wage restraint and access to information.

CONCLUDING REMARKS

1.32 In 1997, the government continued to make progress in improving management processes, particularly related to performance reporting, planning and budgeting. As well, progress was attained toward its goal of balancing annual budgets and establishing fiscal stability. New ways of achieving program objectives within a framework of fiscal restraint were also undertaken with some success. However these initiatives were not without pitfalls and demonstrated the need for careful planning and risk assessment. This was particularly true with regard to the launch of a school construction program. My Office will continue to monitor and report on these initiatives.

1.33 The legislative structure within which organizations are created is sometimes unclear. In previous Reports I have commented on inconsistencies and problems that have been caused as a result. The Atlantic Lottery Corporation and the Highway 104 Western Alignment Corporation were two examples. The Resource Recovery Fund Board Incorporated, reported upon this year, is another example. I urge the Legislature to consider amendments to the Provincial Finance Act and related legislation that would bring clarity to the definition of government entities and the government reporting entity. The applicability of various government policies to all government entities also requires consideration. I intend to undertake a broadly-based review of the organizational status of government entities, their accountability relationships and reporting requirements. This will also focus on the status for purposes of the government financial reporting entity.

1.34 As discussed earlier, this was a year of transition for the Office, with a much earlier reporting deadline and compressed available time and resources. Once again the staff of the Office responded positively and I wish to thank them for their efforts. As well, our deadline put pressure on extremely busy public servants who had to respond to our reports. I thank them for their cooperation.

GOVERNMENT-WIDE ISSUES

2.

ACCOUNTABILITY INFORMATION AND REPORTING

BACKGROUND

2.1 The need for quality accountability information and reporting, including the definition of basic accountability requirements in legislation, has been a topic of consideration in a number of jurisdictions. In its simplest terms, accountability means the obligation to answer for an assigned responsibility. An accountability relationship involves at least two parties, one who allocates or assigns responsibility, and one who accepts it, with an understanding to report upon results or outcomes.

2.2 Exhibit 2.1 on page 20 provides a relatively simple two-dimensional overview of the key elements of an accountability relationship, including the role the audit function serves within it. This overview or model can be used when considering accountability at various levels within Provincial operations. For example:

- government's accountability to the House of Assembly;
- departments' and crown agencies' accountability to government;
- deputy head's or board's accountability to a Minister; and
- management's accountability to a deputy head.

2.3 Exhibit 2.2 on page 20 provides an overview of the accountability organization with respect to the Provincial public sector. It is not intended to present all parties or relationships involved, but rather to emphasize the various levels that exist and that accountability to the public is relevant at all levels.

2.4 The purpose of this chapter is to provide updated summary comments on the quality of accountability information and reporting to the Members of the Legislative Assembly (MLAs), including the Province’s financial statements. Adequate information and reporting on government’s plans and performance (i.e., results or outcomes) are required, so that MLAs can hold government to account.

RESULTS IN BRIEF

2.5 The following are our principal observations this year.

- Progress towards improving the quality of accountability information and reporting by government continued. Nova Scotia has received recognition nationally and internationally for its leadership in regards to its *Planning and Accountability Framework* initiatives, with a specific focus on the annual *Government By Design* publication. The continued provision of such information and reporting to the House of Assembly on a timely basis is discretionary (i.e., not required by statute).

- Improvements made to the Province's financial statements in recent years have resulted in the Province's financial position and annual results being accounted for and reported more completely and understandably than in the past. Certain issues or concerns remain to be resolved, including the preparation of full consolidated financial statements. Finance has indicated its intentions to deal with certain of these matters over time.

- On August 22, 1997, this Office released a Special Report on the Province's non-consolidated financial statements for the year ended March 31, 1997 which had been released publicly by the Minister of Finance.

SCOPE OF REVIEW

2.6 The objective of this assignment was to review the status of action taken or planned to improve the quality of accountability information and reporting to the House of Assembly.

2.7 In addition to considering the status of the *Planning and Accountability Framework* initiatives undertaken by government, we have reviewed and provide commentary on the Province's non-consolidated financial statements included in the *Public Accounts* for the fiscal year ended March 31, 1997.

PRINCIPAL FINDINGS

Nova Scotia Continuing to Demonstrate Leadership

2.8 For the House of Assembly to hold government to account, and for government to hold departments and agencies accountable, there must be an adequate standard framework in place requiring the provision of sufficient, appropriate, understandable and timely information or reports. As indicated in last year's Report, such a standard has been defined and is being implemented in Nova Scotia. The *Planning and Accountability Framework* is a government-wide initiative being coordinated through the Priorities and Planning Secretariat. During 1997, efforts continued to implement the various aspects of the framework and make necessary improvements. The information and reporting documents prepared (or to be prepared) as a result of the framework provide (or are to provide) an increased focus on defined outcomes at an overall government level as well as at the entity or program levels.

2.9 The elements of the framework in place, coupled with those in progress or planned, put Nova Scotia in a leadership role in relation to public sector accountability. Nova Scotia's leadership in this regard has received increased recognition nationally and internationally, including specific focus on and interest in the government's annual *Government By Design* publication. The effective implementation of such information and reporting mechanisms represents a significant challenge, requiring a sustained commitment by government.

2.10 Certain significant accountability-related statutory amendments or provisions were put in place in recent years which support the provision of improved and more timely information and reporting to the House. For example, amendments to the Provincial Finance Act (Section 73) now require business plans and other information for crown corporations to be tabled in the House each year.

2.11 The *Planning and Accountability Framework* will support the provision of improved information and reporting on the plans and performance of government, including at the department or agency level. It was indicated that the information and reporting prepared using the framework is (and will be) tabled in the House. In this regard, we note that there is currently no statutory provision requiring such information and reporting to be made available to MLAs.

2.12 The 1997-98 *Government By Design* included the following summary descriptive note on page 2:

> *"...Government By Design is the planning document for government. It lays out the overall plan of government and the specific business plans of departments as well as the fiscal and debt management plans. A crucial aspect of the process is the identification of outcomes/performance measures, both for government and for departments.*
>
> *Fundamental to accountability is the reporting mechanism. The publication Hitting the Targets is the results/reporting document for government. Not only will it report on the financial performance, it will also include the accomplishments of government and the achievement of outcomes for both government and departments. Released in early fall, it will report on the previous fiscal year in a timely, comprehensive, and easily understandable way.*
>
> *We are in a transition year. The outcomes and measures are identified this year in Government By Design; the targets and the reporting will be published in Hitting the Targets. In future years, targets will be published in Government By Design, and the results of how the targets have been achieved will be published in Hitting the Targets.*
>
> *Together, these publications provide Nova Scotians with a clear understanding of what we have accomplished and where we are going."*

2.13 In August 1997, government released part (essentially the financial part including the non-consolidated financial statements, along with other financial and economic performance information) of the *Hitting the Targets* document referred to above. It was indicated to us that the remaining part (that relating to accomplishments of government and the achievement of outcomes) required further editorial review and adjustment in fall 1997, and will now be titled *Nova Scotia Counts* and released in early 1998. In our view, such a delay should not be considered unreasonable, in light of the challenges associated with the initial preparation of such performance reports.

2.14 In addition to the *Government By Design* and *Hitting the Targets* publications, there are various other reports and publications currently available to the MLAs which can either directly or indirectly be utilized for accountability purposes. As noted in previous Reports, some of these are not required by legislation, and as such are available at the government's discretion. In fall 1997, the Priorities and Planning Secretariat had a research study and analysis in process, including consideration of the nature and extent of statutory accountability provisions in other Canadian jurisdictions.

2.15 Annual reporting standards and practices of departments and agencies need to be updated, expanded and strengthened to support the provision of sufficient, appropriate, understandable and timely information on the results or outcomes achieved in comparison to plans. Further, responsibility for monitoring compliance with annual reporting requirements needs to be clearly assigned. The Priorities and Planning Secretariat had a specific research study and analysis undertaken in this regard during 1997.

Action Taken or Planned by the Department of Finance

2.16 Chapter 2 of last year's Report included a number of comments and suggestions relating to accountability information and reporting to the House, including the Province's annual financial statements. In September 1997, Finance management provided us with a copy of their response to the comments included in our 1996 Report that affect that Department. Their response summarized the action taken or planned, assigned responsibility to specific Finance staff, and established due dates and outcomes (i.e., deliverables).

2.17 Appendix 2A on page 21 provides information extracted from Finance's response on matters included in Chapter 2 - *Accountability Information and Reporting* of our 1996 Report. For purposes of the appendix we have included Finance's comments regarding action taken or planned.

2.18 We want to acknowledge that Finance prepared and provided the response to us on their own initiative. It has been very helpful, and in some regards reflects upon the quality or level of organization and control senior management at Finance are working to put in place over their operations.

Audit of the Province's Financial Statements

2.19 Section 65 of the Provincial Finance Act creates an audit reporting relationship which is unique in Canada. Nova Scotia is the only jurisdiction in Canada where the legislative auditor does not audit and provide an opinion on the government's financial statements. The Province's financial statements are audited by a public accounting firm and the auditors' report (opinion) is addressed to the Minister of Finance. The audit opinion in other jurisdictions is addressed to the House of Assembly (or its equivalent).

2.20 This Office has and will continue to place appropriate reliance on the audit of the Province's financial statements as it relates to our mandate defined under the Auditor General Act. We will continue our efforts to monitor the results of this audit function and provide commentary on the overall completeness and adequacy of the Province's financial statements which are included in the *Public Accounts*.

2.21 In recent years, we have made reference to the annual *Management Report* issued by the external firm appointed under Section 65 of the Provincial Finance Act. The *Management Report* resulting from the audit of the Province's March 31, 1997 financial statements, as well as Finance's response to the comments and recommendations therein, were made available to us in September 1997. That report and Finance's response include information on various issues or concerns with respect to Provincial operations, and will be considered during our future planning for related assignments.

Commentary on the Province's Annual Financial Statements

2.22 The Members of the Legislative Assembly (and the public) require financial information on and reporting of the Province's financial position and results - both plans and performance - on a complete, understandable and timely basis. This view is consistent with the recommendations made by the Public Accounts Committee in its sub-committee report which was tabled in the House of Assembly in December 1996. Among other things, that report provides recommendations dealing with improvements to the Province's financial statements, including consolidation and timely release.

2.23 Since 1993, the Report of the Auditor General has included commentary on the Province's annual financial statements, one of government's primary financial accountability documents. While we have previously identified concerns relating to the completeness and adequacy of the Province's financial statements, improvements made to the statements, in the past three or four years, have resulted in the Province's financial position and results being accounted for and reported more completely and understandably than in the past.

2.24 The timeliness of financial reporting by government has been less of an issue, to some extent due to the Minister of Finance releasing the annual *Financial Report* (which has included the traditional non-consolidated financial statements of the Province) in August in recent years. As noted in previous years the release of the *Financial Report* is discretionary (i.e., not required by statute). However, the *Public Accounts* now must be released by December 31, within nine months of the fiscal year end.

2.25 With respect to understandability of the Province's financial statements, it is important to note that they are, by their very nature, a summary, resulting from the selection of alternative accounting policies and disclosure practices. The impact or implication of these selections may not be fully understood or appreciated by other than a well-informed reader. This notwithstanding, one attribute of understandability of which readers should be assured is that of consistency. In situations where the government elects to change accounting policies, the onus is on government to ensure that such changes are appropriate, as well as fully and adequately disclosed in the notes to the financial statements. In most instances, such changes should result in a retroactive restatement of the prior year's comparative data, so that financial statement readers are still presented with information on a consistent and comparable basis.

2.26 Based on our review of the Province's 1997 financial statements and other information available to us, a Special Report was prepared by this Office and released on August 22, 1997. The following concluding remarks were noted on page 5 of that Report.

> "*As previously noted, in recent years various significant improvements have been made to the Province's financial statements. As a result, the Province's financial position and results are being reported more completely and understandably than in the past. In this regard, I acknowledge the decision to stop using an inappropriate accounting practice relating to the recording of capital commitments in the determination of net capital expenditures.*
>
> *Additional opportunities for improvements to the Province's financial statements and related disclosures have been identified - by Finance, this Office, and others - for future consideration by Government. Nothing short of full and complete accounting for and reporting of the Province's financial position and results should be considered acceptable.*
>
> *My Office will continue to provide appropriate independent commentary on and support for efforts to improve the Province's financial statements and other accountability information and reporting."*

2.27 Finance's commitment to further improve the Province's financial statements is evident, not only by recent initiatives and changes, but also in the Department's section of the 1997-98 *Government By Design* where one of its priorities is noted as to *"...continue efforts toward enhanced corporate understanding and compliance with (PSAAB) guidelines"* (page 83). The *"PSAAB guidelines"* refers to the public sector accounting recommendations of the Canadian Institute of Chartered Accountants (CICA).

2.28 Finance is working on certain matters with respect to the Province's financial statements, including those listed in Appendix 2B on page 24, and has indicated its intentions to address these over time. Depending on how and when some of these are resolved, they may affect the Province's financial position and results reported for the fiscal year ending March 31, 1998.

CONCLUDING REMARKS

2.29 An effective accountability framework should provide or result in an appropriate balance of information and reports to the House of Assembly on the plans and performance of government overall and individual departments or agencies, both from a financial and a program delivery or service perspective. The goal is better information and reports, not just more.

2.30 There have been a number of significant initiatives undertaken to improve the quality and timeliness of information and reports available on the government's plans and priorities. The Department of Finance and the Priorities and Planning Secretariat have taken, and are still planning to take, steps to improve the nature and quality of the information and reports available, including an expanded focus on results and outcomes of departments and agencies in key areas.

2.31 Despite some specific concerns and acknowledging that further improvements will be necessary, the overall quality (i.e., in terms of completeness and understandability) of the Province's financial statements and related reporting is now much better than it was in the past.

Exhibit 2.1

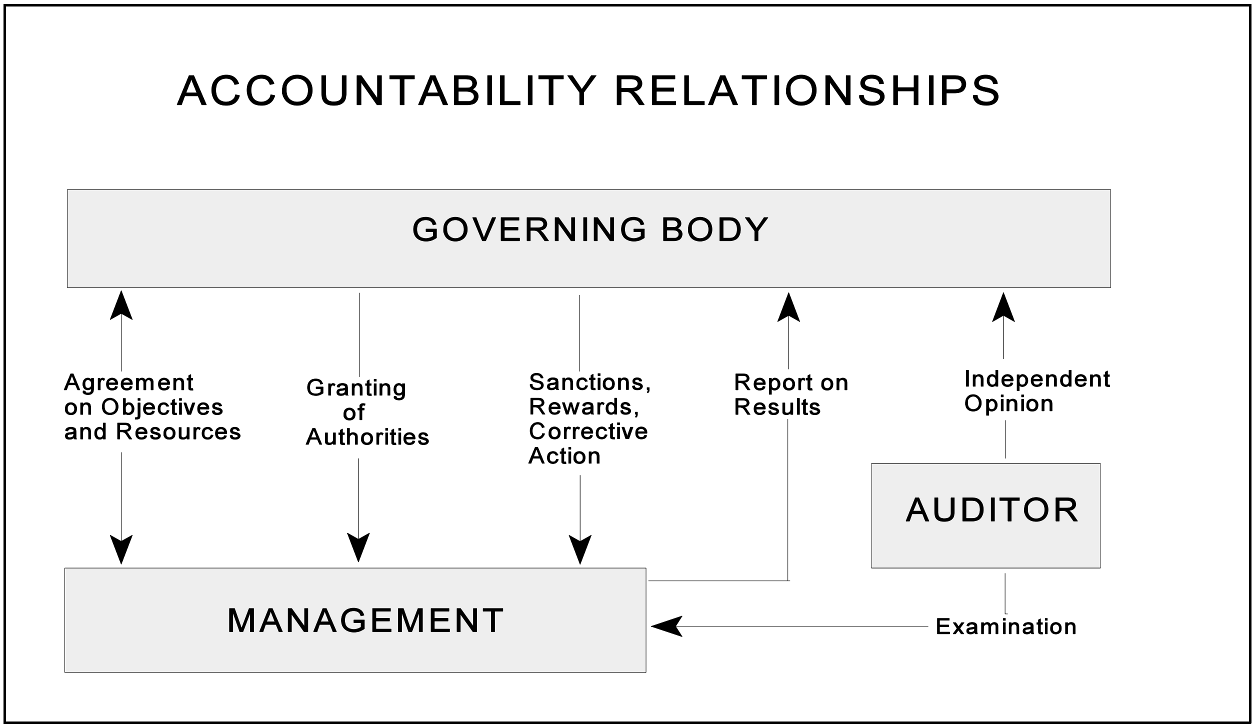
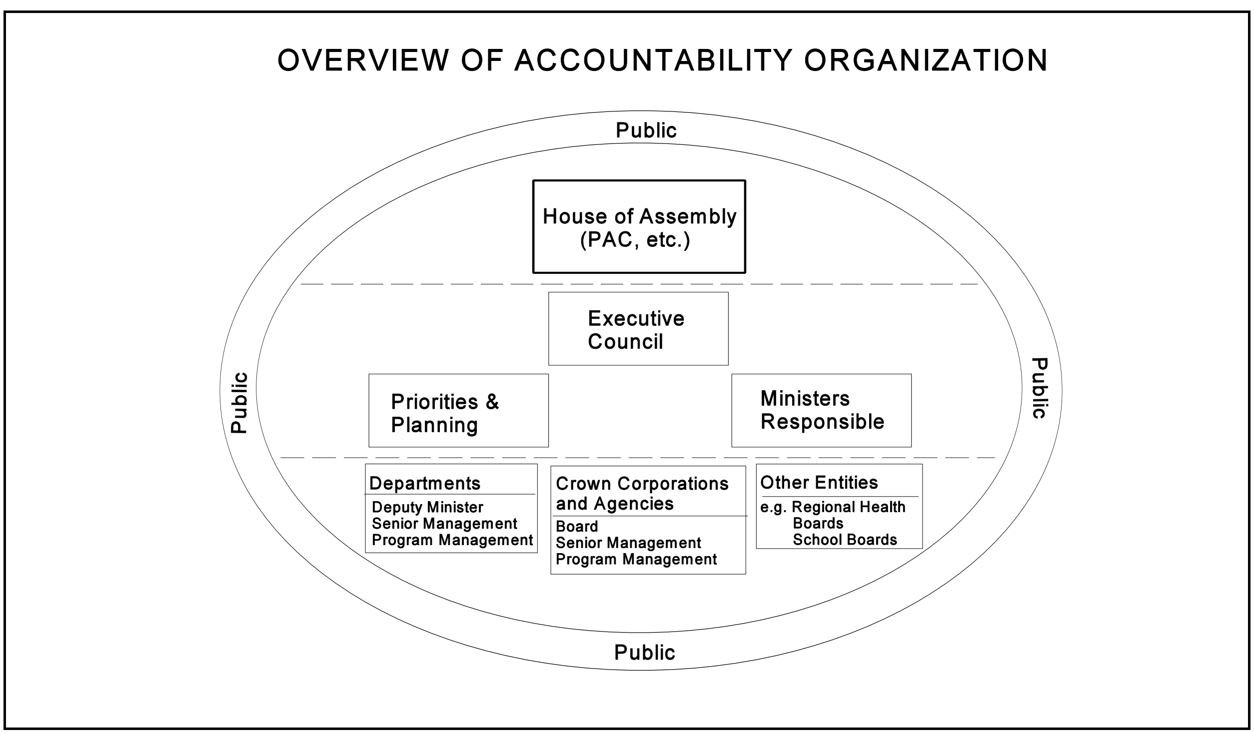


Exhibit 2.2



Appendix 2A

Follow-up to Chapter 2 in 1996 Auditor General's Report Summary of Action Taken or Planned Extracted from Finance's September 1997 Response		
Par. #	**Office of the Auditor General's Comments or Recommendations**	**Summary of Action Taken or Planned**
2.14	...consider the various recommendations included in the PAC Sub-Committee report...	
	vi - timely interim reporting against plans, budget	*Quarterly Reports published.*
	vii - Public Accounts supplement should include information for crown corporations, agencies and other Provincial public sector entities.	*We will be evaluating the Public Accounts presentation and contents for the reports for the year ended March 31, 1998.*
	viii - additional appropriations, warrants reviewed by the House on a timely and effective basis	*Shared reponsibilities with Departments. Completed when information is available and the department and Finance are comfortable that the authority is required.*
	ix - consolidated estimate or budget information with comparison to actual	*Will consider as we look at preparing consolidated financial statements. Consistency of fiscal years may be a problem.*
	x - adopt PSAAB recommendations	*Ultimately, it is the Province's intention to comply with PSAAB, however, this will require much analysis and planning.*
	xi - annual surplus/deficit should be the only change in net direct debt, in the absence of extraordinary or retroactive adjustments	*This recommendation will be evaluated as the Province considers each PSAAB recommendation individually.*
	xii - amend Provincial Finance Act so Public Accounts are released with Financial Report, or at least within nine months of year end.	*The Public Accounts (Volumes I and II) for the year ended March 31, 1997 will be available for release by December 31, 1997.*
2.25	...the issues of full consolidated financial statements and certain costs and other adjustments being charged directly to the *Statement of Net Direct Debt* rather than being reported on the *Statement of Revenue and Expenditures* as part of the annual surplus or deficit...Nothing short of full and complete accounting for and reporting of the Province's surplus or deficit and its liabilities should be considered acceptable.	*The Province will continue to provide supplementary consolidated financial information.* *We will consider preparing fully consolidated financial statements as part of our review of PSAAB recommendations and determine a conversion plan at that time.*

Par. #	Office of the Auditor General's Comments or Recommendations	Summary of Action Taken or Planned
2.28	...where the government elects to change accounting policies...ensure that such changes are appropriate...fully and adequately disclosed in the notes to the financial statements...in most instances, such changes should result in a retroactive restatement of the prior year's comparative data...	*Accounting changes are disclosed in the notes to the financial statements.* *Retroactive application will be considered in instances where the information is readily available.*
2.31	Provide the following comments for consideration:	
	■ Consolidated financial information, and preferably full consolidated financial statements, should be available publicly at the same time as the traditional non-consolidated statements.	*In theory, this is beneficial. In practice, consolidated financial statements will require a lot of effort. Since our resources are limited, the emphasis over the short term will be on timely release of non consolidated F/S until the preparation of consolidated financial statements is well established.*
	■ The Workers' Compensation Board of Nova Scotia (WCB) and Halifax-Dartmouth Bridge Commission have not been accounted for as part of the Province's consolidated reporting entity.	*The Workers' Compensation Board is not part of the Government Reporting Entity. We will evaluate the Bridge Commission to determine if it should be part of the reporting entity.*
	■ Significant adjustments recorded directly to net direct debt for purposes of the non-consolidated statements have not been included in the consolidated (i.e., total) surplus or deficit of the Province reported in the *Consolidated Financial Summary*.	*This will be reviewed as a component of PSAAB compliance as we move toward fully consolidated financial statements.*
2.35	Finance needs to clearly define its accounting policy on what will be recorded directly to the *Statement of Net Direct Debt*...we strongly recommend that, in the absence of extraordinary or retroactive adjustments due to changes in accounting policies, the annual surplus or deficit should be the only factor causing a change in the Province's net direct debt. All other items should flow through the *Statement of Revenue and Expenditures*, and be included in the determination of the reported surplus or deficit for a fiscal year.	*This will be reviewed as a component of 2.31.*
2.36	Completeness of reported liabilities - WCB unfunded actuarial liability should be reported.	*The only liability is the self-insured portion.*
	WCB - Province's liability as a self insurer should be reported.	*It was reported at March 31, 1997.*

Par. #	Office of the Auditor General's Comments or Recommendations	Summary of Action Taken or Planned
2.37	Timely release of consolidated financial statements.	*Public Accounts to be released December 31, 1997 and will contain consolidated financial summary information.*
2.38	Public Accounts released prior to December 31.	*Volumes I and II to be available for release December 31, 1997.*
2.41	Accrual of commitments of $50 million inappropriate	*This has been debated.*
15.14	Public Accounts do not include all entities owned or controlled by the Province.	*This will be evaluated for the Public Accounts for the year ended March 31, 1998.*
17.6	Additional Appropriations/Special Warrants	
	- Expenditures were incurred before the approvals were received	*Until finalization of year end it is difficult to implement. As well, department and the Department of Finance want to be comfortable with amounts to ensure authority is required.*
	- Need to clarify the provisions of the Expenditure Control Act	*In 1997 session some clarifications were made.*
	- Special warrant approved for the Innovation Fund which could have been more appropriately dealt with in the Estimates.	*The Innovation Fund is a revolving fund. Expenditures from the Fund are authorized by BTAC and Departments have to repay the Fund at terms predetermined by BTAC.*

Appendix 2B

PROVINCE'S FINANCIAL STATEMENTS
SUMMARY OF OPPORTUNITIES FOR IMPROVEMENT

Consolidated financial statements - Full consolidated financial statements for the Province should be a primary financial accountability report for government. Consolidated financial information, and preferably full consolidated financial statements, should be available publicly at the same time as the traditional non-consolidated statements. Finance has indicated that it is considering consolidated budget information as part of the move to full consolidated financial statements.

Reporting entity - Finance is reviewing the Province's reporting entity for financial statement purposes. Among other considerations, this initiative will assess whether specific Provincial public sector entities are to be included in consolidated financial reporting, and which ones will be accounted for as government organizations or alternately as government enterprises.

Reporting of annual results - Finance needs to clearly define its accounting policy on what will be recorded directly to the *Statement of Net Direct Debt.* In this regard, it is recommended that, in the absence of extraordinary or retroactive adjustments due to changes in accounting policies, the annual surplus or deficit should be the only factor causing a change in the Province's net direct debt. All other items should flow through the *Statement of Revenue and Expenditures*, and be included in the determination of the reported surplus or deficit for a fiscal year. It is acknowledged that implementing such a policy would represent some further challenges to the annual budget preparation process. Finance has indicated that this is the reporting basis it intends to move towards over time.

Accounting for tangible capital assets - Alternatives and issues relating to the implementation of recent recommendations by the CICA on the accounting for and reporting of tangible capital assets by governments are being studied by Finance, with input from this Office and departments.

Accounting for pension obligations - Since 1993, Finance has implemented changes so that government's pension obligations (i.e., liabilities) are more fully accounted for in its financial statements. Finance has previously indicated that since items such as annual or periodic pension valuation adjustments do not lend themselves to accurate and reliable budgeting, it is appropriate for them to be recorded to net direct debt rather than in the calculation of the annual surplus or deficit. While such items may be challenging to determine, both from a budgeting and an accounting perspective, they still represent items that should be considered when assessing the government's fiscal performance.

Change in accounting policies - The disclosed basis of accounting used for the March 31, 1997 financial statements was not fully appropriate in relation to generally accepted accounting principles, due to certain capital commitments being accrued as expenditures for the fiscal years ending March 31, 1996 and March 31, 1997. Finance has indicated that this accounting practice will be changed for the fiscal year ended March 31, 1998, but has yet to indicate if the change in policy will be made retroactively as is appropriate under the circumstances.

3.

PROCUREMENT - FOLLOW-UP

BACKGROUND

3.1 The Government Purchases Act controls the acquisition of goods in government. The Act assigns responsibility for acquisition of goods to the Government Purchasing Agency for the departments of government, and any board, commission or agency of government designated by Executive Council. The Government Purchasing Agency is part of the Procurement Branch of the Department of Finance.

3.2 On January 1, 1996, government released a *Policy on Government Procurement*. The Policy's objective is "*to establish and maintain a high level of confidence in the procurement process by ensuring that procurement is carried out in an open, fair, consistent, efficient and competitive manner*." The text of the objectives section of the Policy has been reproduced as Exhibit 3.1 on page 32. The Policy applies to all departments, agencies, boards and commissions effective January 1, 1996. Provincially funded public-sector entities such as academic institutions, school boards, hospitals (ASH Sector) and crown corporations must follow the policy effective June 1, 1996. The Policy does not apply to municipalities. According to the Policy "*The Minister of Supply and Services is responsible for promoting and implementing this policy.*" This responsibility was subsequently assigned to the Department of Finance through its Procurement Branch.

3.3 The strategic plan of the Procurement Branch states:

> "*The Procurement Branch has responsibility for ensuring the acquisition of goods, services, construction and facilities by government departments, agencies, boards and commissions is conducted in a manner which is open, fair, consistent, efficient, and competitive. The role of the Procurement Branch is to provide operational assistance in procurement activity; to formulate and advise on policies and procedures governing the procurement process; to assist the municipalities, academic institutions, school boards and hospitals in their procurement activities; to coordinate, with the ERA* [Department of Economic Development and Tourism]*, the negotiation and administration of trade agreements as it relates to the public procurement function; to improve the procurement process by establishing quality assurance and standards for the acquisition of commodities and services; and to build public confidence in the integrity of public sector procurement processes.*"

3.4 The Procurement Branch is also responsible for managing the cooperative business solution (CBS) procurement process which is designed to assist departments in finding solutions to well defined business problems for which they have no preconceived solution. A supplier is selected, on the basis of qualifications and capability rather than price, to form a business alliance of shared risk, resources and benefit between the supplier and government. The challenge is to ensure there is an appropriate policy and control framework to support a fair and open process and ensure fair value is obtained.

3.5 Resource constraints have made it necessary for government to explore alternatives to provide high quality services to the public and develop modern infrastructures. Public-private partnering (P3) has been identified as one means of achieving this goal. P3 is characterized by the government and a private sector organization establishing a formal relationship that shares the costs, risks and rewards on a project. Once it is decided to enter a P3 arrangement, the potential partners are identified through a procurement process. Whatever process is followed, it is important that the objectives of the *Policy on Government Procurement* are met to ensure an open and fair process. The Department of Economic Development and Tourism (ED&T) was responsible for coordinating P3 for government. Subsequent to our review, the Priorities and Planning Secretariat recommended that the Department of Transportation and Public Works assume a larger role with respect to this responsibility.

3.6 Our 1996 Report included a chapter on the results of our review of internal controls established for the procurement function in government, including CBS, and policies and guidelines established for P3. In November 1997, we completed a follow-up review to obtain information on the status of action taken or planned with respect to the various comments and suggestions included in last year's Report.

RESULTS IN BRIEF

3.7 The following are the principal observations resulting from this assignment.

- The Procurement Branch continues to take significant steps to improve controls over the procurement process. The Branch has taken action on all the opportunities for improvements identified in our Report last year. The implementation of formal reporting on procurement activities and exceptions is to be in place by March 31, 1998.
- Steps have been taken to address the need for a strategy and guidelines for managing P3 within government. However, at the time of our review, further steps were required. A division within the Department of Economic Development and Tourism was established to address this need and since its inception, a number of related actions were initiated by the division. Some guidelines have been documented, throughout government, concerning certain aspects of school construction using P3. These could be used to some extent in other P3 projects. The P3 division of ED&T was working on some guidelines relevant to all P3 projects. However, at the time of our review, these were in draft form and did not cover all aspects of the guidelines required. Subsequent to our review, the Priorities and Planning Secretariat recommended the Department of Transportation and Public Works assume a larger role and responsibility for P3 in government.

SCOPE OF REVIEW

3.8 The objective of this follow-up review was to determine the action taken or planned by the Departments of Finance and Economic Development and Tourism to improve controls within the procurement function and P3 activities within government, respectively.

3.9 Our procedures included interviews with selected members of management of both departments and a review of supporting documentation concerning actions taken or planned. We acknowledge the fact that the Department of Finance undertook the initiative to prepare a formal response to observations made in our 1996 Report concerning areas of Department responsibility. This document was beneficial in completing our 1997 follow-up review.

3.10 This assignment did not include a review of compliance with government procurement policies and procedures within specific departments or the ASH sector. This was considered as a potential objective in all assignments undertaken by this Office. Any procurement-related observations are reported in the chapters related to particular assignments.

PRINCIPAL FINDINGS

Management Controls within the Procurement Function

3.11 *Overview* - The Procurement Branch has taken significant steps to design and implement improved controls over the procurement process in the past few years and improvement continues to be an ongoing process. Last year's chapter identified opportunities for further improvements with many of these being addressed through planned activities of the Branch.

3.12 *Policies and procedures* - The establishment of adequate policies and procedures for procurement in government has evolved over a number of years. Prior to the release of the *Government Procurement Policy* in January 1996 there were various policies in government relating to the acquisition of goods and services. However, not all services were covered by those policies, some aspects of the policies were unclear, and there was inconsistency among the policies. The release of the *Government Procurement Policy* in January 1996 addressed these problems.

3.13 The Procurement Branch has taken further steps to ensure a clear understanding by all involved in the procurement process as to processes and procedures to be followed to ensure a fair and open process. This has been done through the creation of numerous publications. As of November 1997, some had been released while others were in draft form. Exhibit 3.2 on page 33 summarizes the list of publications and when they were or were planned to be available as guidelines for government and the ASH sector.

3.14 *Reporting* - In our Report last year, we noted that the total procurement transactions in government were not accumulated and reported and there was no reporting to the House of Assembly or the public of exemptions permitted.

3.15 Effective April 1, 1997, a new corporate financial management system (CFMS) was implemented for government. This system was to provide the accounting information which was lacking. However, the reporting capabilities of this system were not fully operational as of November 1997, so the information was still not available.

3.16 At the time of this follow-up review, the CFMS was also gathering data on exemptions permitted, but staff of the Procurement Branch had been unable to produce reports on this. They were working with others in government in order to obtain this information. It was anticipated that the required accounting and exemption information would be obtained by the end of the 1997-98 fiscal year and would be reported for that year to the Priorities and Planning Committee. No decisions had been made as to whether this information would be reported to the House of Assembly. Staff indicated that they will report to whomever government deems appropriate. Chapter 12 on page 126 of this Report provides more information on the CFMS and its implementation.

3.17 *Outcome measures* - At the time of our 1997 review, the Procurement Branch had developed a first draft of the outcome measures against which success in achieving its objectives will be measured. Staff expected the list of measures to be finalized by the end of the 1997-98 fiscal year with tracking systems to be in place for each measure.

3.18 *Vendor complaints* - During last year's review, in all instances examined, follow-up action on vendor complaints was appropriate and timely. We did however recommend creation of a formal tracking and reporting process to support improvements in accountability and the overall control framework of procurement activities.

3.19 As at November 1997, a draft policy addressing this issue had been developed with the intention of implementing it in 1998-99. There have also been improvements in the flow of information to management of the Branch in relation to the number, type and action taken on complaints received.

3.20 *Procurement of services* - Responsibility for the procurement of services has largely been delegated to departments. Some opportunities for improvement in controls were identified last year. The implementation of CFMS along with the completion of other actions identified by the Procurement Branch should address the opportunities identified. It was indicated that these actions will be completed in 1997-98.

3.21 *CBS guidelines* - Last year the Procurement Branch undertook an internal review of the CBS process to identify any weaknesses and recommend changes to the guidelines to improve the efficiency and effectiveness of the process. We agreed with the recommendations covered in the report resulting from the internal review and identified additional concerns for management consideration.

3.22 In October 1997, the Branch released revised CBS guidelines which address all the areas of improvement identified by the Branch and our Office. These new guidelines should improve the opportunity for obtaining fair value through CBS projects.

3.23 *Additional comments and observations* - The Procurement Branch has undertaken an important initiative this year towards ensuring compliance with the *Government Procurement Policy* throughout government.

3.24 The Policy notes that all procurement activities will be subject to audit by the Auditor General and departmental internal auditors. Compliance with the *Government Procurement Policy* is not always included in the scope of our assignments due to other priorities. However, it is important that an appropriate and active audit function be in place to ensure compliance across government.

3.25 The Procurement Branch recognized this need and contacted the internal audit group at the Department of Finance. With input from the Branch, an audit program has been developed through a Provincial internal audit committee. It is hoped internal audit staff throughout government will use this program, as a guide, to review procurement transactions in the departments for which they are responsible. We support the initiative of the Branch to ensure government is complying with the *Government Procurement Policy*.

Public-Private Partnering

3.26 *Overview* - Many definitions have been put forward for public-private partnering (P3). The following are three representative definitions.

> *"A cooperative venture between the public and private sectors, built on expertise of each partner, that best meets clearly defined public needs through the appropriate allocation of resources, risks and rewards."* (Canadian Council for Public-Private Partnerships)

> *"A public-private partnership (P3) is any situation where the costs, risks and rewards for infrastructure development, or the provision of services are shared by the government and the private sector."* (Slide presentation by Nova Scotia government representatives)

> *"A public-private partnership (PPP) is simply the ongoing participation of an entity, other than the municipality, in providing public infrastructure or services. PPPs share the risks and rewards between government and those who are willing and able to shoulder the burden."* (Public-Private Partnering in the Nova Scotia Municipal Context)

3.27 Whatever definition is used, the key element of a P3 is the sharing of risks and rewards by government and the private sector.

3.28 Government activity in P3 has increased significantly over the past few years and government intends to expand partnering activities. In the 1996-97 *Budget Address*, the Department of Transportation and Public Works was identified as having lead responsibility for creating new P3 arrangements in the Province. In July 1996 ED&T was assigned responsibility for coordinating P3 in government. The goal in using P3 is to provide government services and infrastructure more quickly, efficiently and/or more cost-effectively, while encouraging sustainable economic growth.

3.29 *Prior year's observations* - In last year's review, we found there were no formal policies or guidelines established with respect to P3 in order for government to maximize benefits and avoid or minimize potential risks involved in these arrangements. Although the circumstances surrounding each P3 may be unique, overall policies and guidelines to be applied to all P3s are required to ensure these arrangements are properly managed.

3.30 We found there was no up-to-date inventory of P3 projects initiated by government. The government is accountable for the results of those projects and as such should be able to provide a list of all projects initiated including the progress and results of the arrangements.

3.31 Both of these concerns were to be addressed through the establishment of a Public-Private Partnering Task Force to champion and guide P3 in the Province. The Task Force was to be in existence for approximately two years. Approval to establish this Task Force was obtained from Executive Council in July 1996 but at the time of our 1996 audit, it had not been established.

3.32 *Actions taken or planned by ED&T* - A new division called "Public and Private Partnerships" was established within ED&T in 1997-98. The division, according to the *Estimates, "Provides leadership and coordination for public-private partnership initiatives across government. Works with other departments and the private sector to develop and enhance expertise in public-private partnering."* This division was to fulfill the responsibilities originally approved for the Public-Private Partnering Task Force.

3.33 An Executive Director for the division was appointed in July 1997. At the time of our review there was a co-op student working within the division but no other staff had been identified. After the Executive Director's appointment a number of actions were initiated by the division including:

- A P3 interdepartmental committee with representatives from most departments was established. Its first meeting was in November 1997. The purpose of this committee is to serve as a networking mechanism and source of information on P3 for departments. Through this committee all departments are to be made aware of projects being done and studies being undertaken throughout government.
- A library of information on P3 was initiated so any individual throughout government wanting a question answered or research completed on P3 could contact the P3 division of ED&T.
- An inventory of P3 projects which have been undertaken in the last few years was started. The inventory consists of a list of project names along with an indication of the stage of the project. No decision had been made as to information to be collected on each project.

- A draft document was prepared to serve as a guideline for the process to follow when using P3. It is called *Public-Private Partnership Process*. This document describes the stages to follow from scoping the project to contract monitoring. It identifies key aspects to consider such as the need for a request for qualifications prior to a request for proposals, the content and evaluation of each, and the importance of monitoring the project. There are other guidelines which need to be developed to expand on this one such as the criteria to use in determining projects to be considered for P3 and the need for and content of a post-implementation review. At the time of our review, the division had not made any decisions as to policies and guidelines required to properly manage P3.

3.34 At the time of our 1997 review, it had been almost a year and a half since the proposal on managing P3 in government was approved. As a result, staff of the division were planning to complete a review, with input from other departments, on the P3 process to date and to recommend a new proposal on how best to manage P3 within government.

3.35 *Actions taken or planned by others* - The Department of Finance issued a discussion paper in November 1997 on *Transferring Risk in Public/Private Partnerships*. The P3 division of ED&T was not involved in this initiative because it was undertaken prior to the appointment of an Executive Director to that division. As noted in the executive summary of that discussion paper "*This paper identifies some of the risks found in typical capital projects. It also explores some of the criteria to be used in judging the transfer of such risks. Finally it offers some examples of risk transfer projects and outlines some of the related accounting issues that will arise.*" It centres around the challenges faced by government in implementing P3 to create high tech schools but can be used, to some extent, for other P3 projects.

3.36 In response to a request from the Premier in the fall of 1997, the Priorities and Planning Secretariat and other agencies of government conducted a review of the P3 process followed to date for school construction in the Province. In December 1997, the Priorities and Planning Secretariat released a report on that review including recommended guidelines to improve the process for future school construction and to some extent other P3 projects. We performed an audit of school construction initiated to date through P3. See Chapter 8, page 78 for the results of that audit.

3.37 The recommendations in the Priorities and Planning report include the requirement to:

> "*Assign a coordinator with responsibility for coordination of all public-private partnership projects to ensure consistent management. This senior official should report to the Deputy Minister of Transportation and Public Works and be supported by the appropriate expertise from departments such as Justice, Finance, Transportation and Public Works and such other departments or persons as may be required and designated by the Deputy Minister of Priorities and Planning Secretariat. The coordinator should, as a standard practice, seek private sector legal, business and accounting expertise in respect of each project. Lead departments should be major participants in the project team structured for each project. The coordinator should structure a project team for each project, the makeup of which should be dictated by the type of project, i.e. school, correctional facility, highway."* (Page 7)

3.38 This recommendation shifts responsibility for coordinating P3 in government from ED&T to the Department of Transportation and Public Works.

CONCLUDING REMARKS

3.39 The Procurement Branch has demonstrated a commitment to ensuring fair and open procurement practices in government. Significant improvements in controls over the procurement function have been made in the last few years and improvements continue to be an ongoing process.

3.40 With government activity in public-private partnering increasing in the past few years and the intention to continue to use this process, it is important that an overall accountability and control framework including formal policies and guidelines be established to maximize the potential benefits and minimize the potential risks of public-private partnering. Some progress has been made in addressing these concerns over the past year. However, further work is required and should be done on a timely basis.

Exhibit 3.1

EXTRACT FROM
POLICY ON GOVERNMENT PROCUREMENT

POLICY OBJECTIVE

The objective of this policy statement is to establish and maintain a high level of confidence in the procurement process by ensuring that procurement is carried out in an open, fair, consistent, efficient, and competitive manner.

The Government of Nova Scotia is committed to

- *ensuring that the government's requirements for goods, services, construction, and facilities are met through an open and fair process that provides the highest degree of competition and value to the Province*
- *ensuring that all bidders have reasonable notice and opportunity to tender*
- *fostering economic development by giving every capable Nova Scotia supplier the opportunity to do business with the government*
- *encouraging Nova Scotia businesses to be competitive and to sustain quality product development*
- *adhering to the Agreement on Internal Trade and the Atlantic Procurement Agreement, which create economic opportunities for Nova Scotians*
- *being accountable to the public for procurement decisions*

Exhibit 3.2

POLICIES AND GUIDELINES FOR PROCUREMENT

Document	**Status**	**Date Released or Estimated Release**
Government Procurement Policy	Available	January 1996
Environmentally Responsible Procurement Policy	Available	December 1996
Various Brochures Concerning doing Business with Government	Available	December 1996
Procurement Process (Government)	Available	January 1997
Procurement Process (ASH Sector)	Available	January 1997
Procurement and the Nova Scotia Economy	Available	January 1997
RFP Preparation Guide	Available	January 1997
RFP Evaluation Guide	Available	January 1997
RFP Proponents Guide	Available	January 1997
Guide to Vehicle Rentals	Available	January 1997
Unsolicited Proposals Guide	Available	July 1997
Revised/Improved Cooperative Business Solutions	Available	October 1997
Procurement Manual Policies and Procedures	Available	December 1997
Construction Contract Guidelines	Draft	December 1997
Facilities Procurement Guide	Draft	January 1998
Supplier Complaint and Dispute Settlement Process	Draft	January 1998
Engineering/Architect Procurement Process	Draft	March 1998

4.

INFORMATION TECHNOLOGY MANAGEMENT - YEAR 2000 READINESS

BACKGROUND

What is the Year 2000 issue all about?

4.1 The approaching change of century brings with it a potential realization of significant risks for computers and computer systems world wide. These risks are characterized by the manner in which computers, both hardware and software, had traditionally been designed and programmed to capture, store and process dates. Dates had been captured allowing only 2 digits for the year (i.e., 1997 would typically have been recorded as 97). When the century changes to the year 2000, under the old format the year would be recorded as 00. Computers may then interpret this to be the year 1900. As a result, computations or processes dependent on dates may be performed incorrectly or not at all. This has the potential to cause an innumerable variety of problems for computer systems, their users and clients, ranging from very minor to extremely dangerous or costly depending on the nature of the system, its functional purpose(s) and the extent of dependency by users and clients.

4.2 In the 1960's and 1970's when the proliferation of computerized business applications truly began, computer memory was a scarce and very expensive commodity. Dates were a very common data element being captured and processed and the recording of the year as two digits provided a significant saving in storage space, data entry efforts and associated costs. At the time, it was a valid economical judgement to conserve storage space in this manner.

4.3 In the 1980's and early 1990's knowledge of the Year 2000 problem and its potential consequences became much more apparent. Although the availability and costs of computer memory dropped dramatically, there was still very little done to address the issue. Both public and private sector organizations have been very slow to react and, until very recently, many have failed to make the issue a priority.

How significant is the issue?

4.4 In 1997 the Gartner Group, an independent research firm, estimated the costs to resolve the issue globally in the range of US $300-US $600 billion and further that the problem affects 90% of the world's computers. The deadline for resolving this problem is a fixed target. It cannot be changed, altered or deferred. In fact, the real target for resolving the problem is not even December 31, 1999. Information Technology industry experts indicate that it should be resolved by December 31, 1998 since many problems will begin to surface in 1999, or earlier where future dates are recorded and processed. That only leaves one year to get the work done, since 1999 is also generally viewed as a year to complete testing and resolve new problems that may surface from the Year 2000 changes.

RESULTS IN BRIEF

4.5 The following are our principal observations.

- The Year 2000 issue represents a very real threat to government and its ability to provide complete and uninterrupted service upon the turn of the century. The issue has a fixed target for resolution which cannot be altered or changed.

- The Nova Scotia government is to be commended for the steps which it has already taken or planned to address this issue. However, there is still much left to do and a rapidly diminishing window of opportunity to complete the necessary tasks. The government must fully consider the risks and ensure sufficient resources are allocated to enable the timely resolution of the issue.

- The scope of the central Year 2000 Project Office addresses only the eight corporate service units and their departments as well as a few small entities. Excluded from the project are many public sector organizations or entities such as crown corporations, school boards, museums, community colleges, hospitals and regional health boards as well as many other government-sponsored boards and commissions. There is no government-wide mechanism in place to monitor, support and coordinate the activities of these organizations in their efforts to achieve Year 2000 compliance.

- There were significant delays in establishing the Project Office which were a result of budget-related deliberations. These deliberations also resulted in departments being required to fund Year 2000 projects from existing budget resources.

SCOPE OF REVIEW

4.6 The objective of this assignment was to review the status of actions taken or planned to address the potential risks and impact that the change of century may have on the deployment and use of information technology resources in the Nova Scotia government.

4.7 Due to the significance of the Year 2000 issue and implications for the Province's information technology systems and controls, we will continue to monitor and review government progress in this regard.

PRINCIPAL FINDINGS

What has been done to date to address the issue?

4.8 The Nova Scotia government, like all other Canadian governments, has a wide variety of computing resources ranging from mainframe-based systems to desktop computers with a variety of networking linkages including a wide area network and many local area networks. The systems in use provide both operational support applications for government departments as well as applications specific to the delivery of government services and programs. Some of the applications in use were developed many years ago.

4.9 In 1991, the government approved standards in the area of information technology. One of these standards addressed the use of dates in mainframe-based systems and applications. It recognized the requirement for an eight digit date with four digits for the year. All mainframe-based systems and applications developed by the government since 1991 were therefore required to use this new date structure. This standard provided a significant head-start to addressing the Year 2000 issue, however it did not resolve the issue for older or non-mainframe based systems.

4.10 In October 1996, a need was recognized to formulate a strategy to address the Year 2000 issue within the Nova Scotia government. Initially, the following three primary thrusts were identified:

- to inventory all government systems and applications and determine the extent of the problem;

- to provide project leadership and coordinate the efforts of departments and agencies; and

- to communicate the urgency of the Year 2000 issues.

4.11 The Technology and Science Secretariat (TSS) took the lead role in this project. In November 1996 a tender was issued for an initial assessment of the problem across the Nova Scotia government. This resulted in a contract to a consulting firm to do the initial assessment. The work was performed over the next several months through the use of survey questionnaires combined with follow-up interviews. In March 1997 a report titled *Year 2000 Project Initial Assessment* was released. The consultants tabulated a total of 280 applications government-wide and concluded that *"Overall, Year 2000 compliance within the computer applications looks good.*" This assessment was based on the following results:

- 43% of applications were already considered compliant;

- 33% of applications required no action as they were in the process of being rewritten, phased out or replaced; and

- 24% of applications required remedial action.

4.12 The remedial action to major applications was estimated by the consultants at between $2.2-$5.3 million of direct expense. The *Initial Assessment* also offered several recommendations in terms of organization and strategy for the project. Government has reviewed these recommendations and most have been accepted. One of the report's primary recommendations centred around the establishment of a central Year 2000 Project Office to coordinate and monitor the efforts of the departments. The departments, through the corporate service units (CSUs), will be responsible for the actual performance of the work.

4.13 The Project Office will also establish a central testing and certification facility where departments will be able to have their applications tested and certified. The Project Office, in consultation with the CSUs, will prioritize the 280 applications and provide certification services for all critical applications as a minimum. To the extent that time and resources permit, they will provide certification for as many more applications as possible.

4.14 However, as noted in paragraph 4.20, a separate budget for this project was not approved. It has been indicated that if alternate sources of funding cannot be identified for the testing and certification process, which is currently estimated to cost $1 million, it may become necessary to allocate and recover these costs directly from government departments and participating agencies.

4.15 In October 1997, the Deputy Minister of the Technology and Science Secretariat wrote to all Deputy Ministers concerning the Year 2000 and its budget implications. He stated in part "*The Technology and Science Secretariat has identified Year 2000 as a serious issue for government and that all departments should make this potentially disastrous problem a priority as well*".

What is the scope of the government's Year 2000 project?

4.16 Although the Year 2000 project is described as a government-wide project, this is not really the case. It addresses only the departments and agencies covered by the eight CSUs, as well as a few other small entities. Excluded from the project are many public sector organizations or entities such as crown corporations, school boards, museums, community colleges, universities, hospitals and regional health boards, municipalities, as well as many other government-sponsored boards and commissions.

4.17 There is currently no government-wide mechanism in place to monitor, support and coordinate the activities of these organizations in their efforts to achieve Year 2000 compliance. Since government has or shares responsibility for these organizations, there should be a means for determining their level of preparedness and the adequacy of their plans for action. One suggestion is to have the government Project Office expand its scope to determine where these organizations stand and include them in the overall project.

4.18 With regards to the hospitals and regional health boards, we were informed that the Department of Health has already taken a leadership role. In a manner similar to the Project Office established in the TSS for the government project, the Department of Health has established a separate project office to monitor and support the efforts of the hospitals and regional health boards. It has been indicated to us that these organizations are well along in the process.

Are there sufficient resources available to do what needs to be done?

4.19 Since the release of the *Initial Assessment* in March 1997, there were delays in proceeding to implement the report's recommendations. An initial schedule was provided that identified the budget and establishment of the Project Office as tasks to be completed by July and August 1997, respectively.

4.20 A great deal of time was spent in attempting to establish a budget for the overall project. It was indicated that a request was made to the Department of Finance for a three-year budget for the project, but approval was not provided due to the budgetary restrictions imposed by the Expenditure Control Act. The Department of Finance position was that the departments would have to fund their Year 2000 projects entirely from their existing budgets. No further funding could be provided.

4.21 The administrative costs associated with the Project Office will now be funded from the budget of the Technology and Science Secretariat. As a result of these delays, the Project Office is only now being established in December 1997, some four months later than planned. In regards to the overall time line, this delay consumed approximately 14% of the remaining time and has placed the project behind schedule.

4.22 It is important to note that at the time of the initial assessment, the Nova Scotia government overall appeared to be fairly well prepared for the new century. However, there is still a significant amount of effort remaining to be completed and it is very possible that departments will have to allocate additional resources (both in dollars and especially people to do the work). Management awareness and commitment to the Year 2000 project is therefore vital. The government must be prepared to allocate necessary resources if significant problems or delays occur.

What is the availability of people with the necessary skills to do the work?

4.23 There is a further related factor that has arisen as a direct consequence of the Year 2000 issue which may directly impact the success or failure of the government's efforts. There is already a growing worldwide shortage of qualified people to manage and perform Year 2000 projects. Lucrative contracts are already being offered (and they will likely become even more attractive as the clock ticks down), particularly in the United States, which has already been actively recruiting qualified people from around the world. These people are virtually leaving their prior organizations stranded because of the high demand and attractive compensation for their skills. The Gartner Group has stated "*Canadian programmers making $25,000 are now being offered 100%-200% raises to come to the US and Great Britain*."

4.24 The Gartner Group, in testimony to the US House of Representatives in November 1997 stated:

> "*Gartner Group believes that less than 15% of enterprises have progressed past the initial assessment and planning stages of their Y2K projects. We expect the remainder to begin the remediation and testing phases in the next six months. Think of it - 85% of the world's enterprises will begin executing the largest IT project they have ever undertaken at virtually the same time! Clearly, there are not enough skilled resources - programmers, data base administrators, project managers, to complete the task in time to avoid damage due to the Year 2000*."

4.25 Government could find itself in a significant bind since they may be unable to compete with the private sector in a bidding war for scarce resources.

4.26 To further illustrate and bring home the seriousness of these global resourcing issues for the Year 2000, and in particular the Nova Scotia government, it is interesting to note that a Request for Proposals (RFP) was recently released and awarded for an experienced Year 2000 Consultant to work with the Technology and Science Secretariat to establish a Nova Scotia government Year 2000 Project Office. Although a qualified consultant was ultimately obtained through this process, there were only four responses to the tender. Two major IT consulting firms of international stature who normally would respond to such tenders were unable to respond to this RFP due to a shortage of resources. As the date draws nearer, this situation can only worsen and the costs could escalate dramatically.

CONCLUDING REMARKS

4.27 The Year 2000 issue represents a very real threat to government and its ability to provide complete and uninterrupted service upon the turn of the century. The Nova Scotia government is to be commended for the many steps which have already been taken or planned. However, there is still much left to do and a rapidly diminishing window of opportunity to complete the necessary tasks.

4.28 As previously stated, the Year 2000 issue has a fixed target which cannot be changed or altered. Time is of the essence and there is no time to ponder or debate the issue further. It is therefore necessary for the government to fully consider the risks and ensure that the resources allocated are sufficient to ensure the timely and adequate resolution of the issue.

4.29 Furthermore, the unique nature of this problem should be of significant and on-going interest to Members of the House of Assembly. Accordingly it would be appropriate that periodic status reports be issued by the Year 2000 Project Office so government and the House may be kept current on progress for this very important issue.

DEPARTMENT AUDITS

5.

DEPARTMENT OF COMMUNITY SERVICES - FOLLOW-UP TO 1995 AUDIT

BACKGROUND

5.1 The 1995 Annual Report of the Auditor General included the results of a broad scope audit of the Department of Community Services conducted in the fall and winter of 1995. In the fall of 1997 we followed up on some of our more significant observations and recommendations relating to the Department's family benefits program.

SUMMARY OF FINDINGS FROM 1995 AUDIT

5.2 The cost of the family benefits program increased approximately $78.7 million (46%) in the five-year period ending March 31, 1995. The increase was primarily due to rate increases, the changing profile of client cases, reductions in Federal income security programs, and increases in the number of family benefit cases. The number of cases increased 21% in the same period. The Department undertook initiatives to control the cost of the program, including establishment of an eligibility review program and consideration of more aggressive collection of overpayments.

5.3 The Department had good management controls in place to enable proper delivery of the family benefits program. However, there was a need to have better access to Provincial data bases to verify clients' eligibility for benefits. We found 25 people receiving benefits who were receiving a government salary or pension which was not accurately reported to the Department. We also discovered 20 individuals who were receiving benefits while serving either a continuous or intermittent term in a Provincial correctional facility.

5.4 The eligibility review program was an effective strategy for detecting errors and improprieties that lead to overpayment of benefits. We recommended expansion of the program. We also recommended having more eligibility review procedures conducted by caseworkers as part of the client intake process. Currently, the program focuses primarily on clients who have already been accepted into the system and are receiving benefits.

5.5 Known accumulated overpayments of family benefits amounted to $24 million. Approximately $16 million related to people no longer receiving benefits and $8 million related to active recipients. Management estimated that there was also $9.6 million of undetected overpayments around the time of our 1995 audit. These amounts were not valued for collectability and recorded in the accounting records of government. Collection efforts were adequate for active recipients, but were inadequate for people no longer receiving benefits. However, the use of a private sector company to collect overpayments was being considered.

PRINCIPAL FINDINGS FROM FOLLOW UP

5.6 *Cost control measures* - The annualized cost of the family benefits program decreased by approximately $22 million (9%) in the 30-month period ended September 30, 1997. The number of cases decreased approximately 9% during the same period. The Department established a Revenue Recovery Unit effective April 1996. The mandate of this unit is to manage existing opportunities and explore new opportunities for family benefit cost containment and overpayment recovery. The unit incorporated the eligibility review program described below. It is estimated by management that approximately $7.2 million in program savings and recoveries were obtained by the unit in the year ended March 31, 1997. The eligibility review program contributed $3.7 million to this total. This is an increase from the $2.9 million reported in 1995 as contributed by the program.

5.7 *Eligibility of applicants for benefits* - In our 1995 audit, we compared the Provincial payroll and pension records with family benefits records and detected instances of income not being reported by family benefit recipients. We also examined Department of Justice files and discovered inmates of Provincial correctional facilities who were receiving family benefits. The Department of Community Services investigated our findings and prepared a report on each instance. The reports note the results of the investigation, whether an overpayment exists, and provide a recommendation on whether to continue or discontinue benefits. However, we found it necessary to further examine certain of the cases as the results of the Department's investigations were sometimes ambiguous. As a result, we discovered two instances where the Department's overpayment calculation was incorrect and another two where it was necessary for the Department to send the file to the Department of Justice for fraud investigation.

5.8 The Department has not expanded its information sharing agreements to include Provincial data files relating to public service salaries, pensions or prisoners in Provincial jails. According to discussions with management, they believe the cost of such efforts would exceed the overpayments that could be recovered.

5.9 Our 1995 Report also recommended sharing of information with other government agencies and with other provinces. The Department could not do this with Nova Scotia Vital Statistics as its records are not yet computerized. The Department has not negotiated an agreement with the Department of Education and Culture to gain access to student assistance information. The Department has finalized an agreement on sharing income assistance program information with the Province of Ontario, and is in the initial stages of negotiating an agreement with the Province of Prince Edward Island. No dialogue with the government of Newfoundland has been initiated yet.

5.10 Management has informed us that it will be more beneficial to obtain an agreement with Revenue Canada to access Federal income tax records, and they have been focusing much of their efforts on trying to finalize this arrangement. However, issues pertaining to confidentiality and commonality of access among the provinces must first be worked out with Revenue Canada. The Department has also expanded its access to Employment Insurance files maintained by Human Resource Development Canada (HRDC). At present, all district offices of Community Services can access these files to determine if applicants are receiving employment insurance benefits. In some areas of the Province, Community Services and HRDC share office space to make cooperation more effective.

5.11 *Eligibility review program* - The Department has expanded the number of eligibility review officers to eleven, from the eight reported in our last audit. These new positions are located in the three amalgamated municipalities of Halifax, Queens and Cape Breton. The work of these individuals is still not part of the client intake process, but is aimed at individuals who have already been accepted into the family benefits program and are currently receiving benefits. However, the Department is in the process of setting up a pilot project in the Halifax Region which will have eligibility review officers included in the client intake process. Based upon the evaluation of this project, it may be implemented on a Province-wide basis.

5.12 The Department is also subsidizing the wages of 14 eligibility review officers who function as part of the client intake process in the municipalities. Management indicated that the municipalities have found this position to be effective in preventing inappropriate payment of benefits. When the Department takes over responsibility for all social assistance in the Province on April 1, 1998, it wants to retain these positions.

5.13 *Overpayment of benefits* - Accumulated overpayments as at September 30, 1997 totalled approximately $35 million, which is an increase of $11 million over the $24 million calculated as of October 31, 1995. This was comprised of approximately $10 million (1995 - $8 million) for active recipients and $25 million (1995 - $16 million) for recipients who are no longer collecting benefits. It is the practice of the Department not to write off overpayments, so that if individuals owing money to the Province apply for benefits in the future, the overpayment can be applied against any benefits paid. As a result, the $25 million noted above represents overpayments that go back to 1952.

5.14 Management explained to us that the $11 million increase is partly due to expanded effort towards reviewing the eligibility of benefit recipients, both at intake and through the work of the Revenue Recovery Unit. In 1995 we reported that the Department estimated $9.6 million of undetected overpayments in the family benefits caseload population at any one time. Management believes that, due to the eligibility review program, total undetected overpayments have been reduced. However, the estimate has not been updated.

5.15 In 1995 we reported that antiquated computer systems were partly responsible for benefit overpayments. The Department has developed and continues to develop computer systems for the recording, paying and reporting of income assistance. Completion is forecast for May 1998. As described in our 1995 Report, income assistance is the program that is replacing the family benefits program. It is currently in effect in the regional municipalities of Halifax, Cape Breton and Queens, and will be implemented throughout the Province by April 1, 1998. No changes are being made to the old family benefits computer systems as they will be removed from service when the income assistance program takes over.

5.16 Annualized overpayment recoveries from active cases at September 30, 1997 were approximately $2.9 million, which is an increase from the $2.5 million estimated in 1995. In February 1997, the Department started a one-year pilot program with the Provincial Department of Business and Consumer Services to collect overpayments from people who are no longer receiving benefits. The Department now issues two letters requesting payment and if no response has been received after 60 days, collection responsibility is turned over to the Department of Business and Consumer Services. The Department of Community Services is in the process of evaluating the results of this agreement. Preliminary results indicated approximately $250,000 was collectable. This amount was recorded in the accounting records of the Province as a receivable as at March 31, 1997.

5.17 We previously reported that greater use of technology by caseworkers would likely result in more efficient management of their caseloads. We also reported that caseload reporting was inadequate in certain areas, and that the Department planned to have new management information systems completed in 1996. New systems were implemented to give staff access to the information they need with respect to the family benefits and income assistance programs. The new systems have not yet been expanded to give caseworkers remote access to the systems from other than Community Services offices. However, this possibility is being explored.

CONCLUDING REMARKS

5.18 The results of our 1995 audit were presented to the Department of Community Services in February 1996. Our follow-up review was commenced 18 months later in September 1997. We found that the Department has made progress in addressing most of our recommendations, especially those relating to the eligibility review program and overpayment collection.

5.19 We also recognize that the Department has been involved in a large and complex project aimed at reforming social assistance legislation, policy and processes. The project is very time-consuming as it involves a number of stakeholders and significant change to the social assistance mandates of both the Province and all Nova Scotia municipalities. Also, some of the issues being addressed in social assistance reform may affect how the Department acts on some of the findings we have reported.

DEPARTMENT OF COMMUNITY SERVICES' RESPONSE

The Department of Community Services acknowledges with appreciation the follow-up report of the office of the Auditor General to the 1995 broad scope audit. We are pleased that this follow-up recognizes the significant work underway within the department related to items specified in the 1995 audit, as well as major initiatives.

The Department of Community Services' single most important initiative in Income and Employment Support Services is the comprehensive restructuring of social services in Nova Scotia. This system has not had the benefit of a comprehensive review of this magnitude for more than thirty years. This initiative has two main components:

- *the disentanglement of the two-tier system of municipal and provincial delivery to create a single-tier provincially delivered system;*
- *the development of new, updated policies underpinned by new legislation.*

A Project Team with dedicated staff resources has been established to manage the restructuring initiative. The team includes four regional representatives who lead regional planning groups, working with the Regional Administrators in the planning and development of regional delivery.

The audit report further recognized the technology changes instituted by the department beginning with the provincial takeover in the Cape Breton Regional Municipality which saw the takeover of municipal social assistance by the province in August 1995. Technology was expanded and enhanced as the delivery of social assistance in Halifax and Queens Regional Municipalities was assumed by the province on April 1, 1996. The Department will have the benefit of this enhanced technology system effective April 1, 1998, when the transfer of the remaining 52 municipalities is complete. In addition, this new system will better serve the existing Family Benefits program when its 30,000 clients are migrated to it in June of 1998. The audit report supports the direction to concentrate resources on these technology changes rather than changing a system which in the near future will be shelved.

The audit report also notes the significant contribution of the Revenue Recovery Unit in improving overall efficiency and effectiveness.

Further support is provided in the audit report for the need for concentration of resources dedicated to tape matching to areas of greatest yield. The example provided in the audit report on the four-case yield from a match on payroll, pensions, and correctional facilities supports our resource allocation to higher yield tape matching initiatives, such as Revenue Canada, which would be applicable to all cases in the system.

The audit report notes the importance and level of financial support provided by the Department in the area of Eligibility Review. The audit also makes reference to the accumulated overpayments (dating back to 1952) which now total approximately $35 million and the Department's increased efforts at both avoiding overpayments through strategies like Eligibility Review and collecting those overpayments now on the books where this is realistically possible, without causing undue hardship. What may not be clear is that increased overpayments in the system being detected, recorded and pursued is the positive result of an improved control system.

6.

DEPARTMENTS OF COMMUNITY SERVICES AND HEALTH - HOMES FOR SPECIAL CARE - PHASE 1

BACKGROUND

6.1 The Homes for Special Care Act governs many long-term care facilities throughout the Province including nursing homes, homes for the aged, homes for the disabled, and residential care facilities. Individuals in these homes may have assistance from the Departments of Health and Community Services for the payment of per diems as provided for under the Social Assistance Act. The Department of Community Services also funds residents in smaller facilities under a program referred to as Community Based Options (CBO). CBO homes are not governed by the Homes for Special Care Act. However, the Department of Community Services released Interim Standards on November 26, 1996 to provide a measure of control over these facilities.

6.2 Individuals are admitted to these facilities as the result of an assessment and classification process. Assessments and classifications are performed by staff of the Departments of Community Services and Health, based on information collected and recommendations made by caseworkers. In some municipalities, caseworkers are employed by the municipality. In the amalgamated municipalities of Cape Breton, Halifax and Queens, caseworkers are employees of the Department of Community Services. In yet other municipalities, caseworkers employed by the Department work on a contract basis for the municipality. It is anticipated that all caseworkers will be employed by the Department of Community Services on April 1, 1998 when the Province assumes total responsibility for social assistance in Nova Scotia.

6.3 *Facilities* - The Department of Health provides financial assistance through its Long-Term Care Program to residents in nursing homes or homes for the aged. A total of 69 of these facilities are licensed by Health throughout the Province representing approximately 5,800 beds. At any time residents occupying approximately 75% to 80% of these beds are financially subsidized by the Department through payments to the homes. These payments are based on approved per diem rates for each home, which averaged $91.61 as at May 1, 1997. These facilities may be municipally-owned, private non-profit or private for-profit entities. There are also long-term care beds in several hospitals in the Province.

6.4 The Department of Community Services licenses the homes for special care for which it is responsible, including rehabilitation centres, residential care facilities, group homes, adult residential centres and developmental residences. At July 31, 1997 there were 117 of these homes containing 2,608 licensed beds. CBO homes are unlicensed, and at July 31, 1997 there were 440 homes with 1,176 residents. As with nursing homes and homes for the aged, the facilities licensed by Community Services are owned by a variety of groups. The Department has indicated there has been a moratorium on new licenses for homes for special care under its jurisdiction for four years and on the development of new CBO homes accepting publicly-funded residents for two years.

6.5 *Financing* - Financial assistance for residents of all homes for special care, including nursing homes and homes for the aged, was provided through funding from the Federal government, municipalities and Community Services until April 1993. At that time the responsibility for nursing homes and homes for the aged was transferred to Health and the funding was shared between the Province and the municipalities. Under Provincial Municipal Service Exchange which took effect

April 1, 1995, the Province assumed responsibility for a greater portion of the costs associated with these residents. Some funding from the municipalities remains.

6.6 The budget for the Long-Term Care Program at Health is based on the net cost of maintaining residents in nursing homes and homes for the aged. The total amount approved by the Department of Health as the budget to operate nursing homes and homes for the aged for 1997-98 was approximately $199 million. Of this amount, about $90 million is contributed by residents of these facilities toward the cost of their care. The remaining $109 million is funded by Health and is included in the 1997-98 Estimates for the Department.

6.7 Community Services provided $44 million for residents of homes for special care under its jurisdiction for the year ended March 31, 1997. Community Services has also been funding municipalities for CBO homes since April 1995 and incurred expenses of $29 million for residents in these facilities in 1996-97. Municipalities pay CBO homes an established per diem for residents and claim the full amount from Community Services. Estimates for 1997-98 are $47 million and $31 million for homes for special care and CBO homes respectively.

RESULTS IN BRIEF

6.8 The following are the principal observations from this audit.

- The Acts and regulations provide a broad framework for policies dealing with classification and assessment, however, policies for a number of areas related to homes for special care need to be standardized throughout the Province. The lack of standardized policies has led to inconsistencies in current practices across the Province. The Community Supports for Adults Policy Committee has been established jointly by the Departments of Community Services and Health to work on Provincial standards to promote consistency.

- The Social Assistance Act provides some guidance on issues surrounding designated residences but the results of our audit indicate possible inconsistency in the application of these guidelines throughout the Province because there are no Province-wide administrative policies in certain areas. A consistent policy is required to ensure proceeds upon sale of designated residences and rental income from such properties are treated consistently. We have recommended that policies surrounding designated residences be expanded.

- Standard procedures for verification of financial information obtained from residents should be developed. In addition, practices with respect to the amount and type of assets which may be retained by an individual upon entry to a home for special care need to be made more consistent.

- Individuals are classified to the level of care required by that person. These levels of care are clearly defined in the Provincial Classifications and Assessments Manual.

- Periodic reviews of residents' care needs or financial situations are not being conducted frequently enough, as required by the Classifications and Assessments Manual, to determine if changes are needed to the original classification or assessment of financial need. We have recommended that the Departments of Community Services and Health clarify the roles and responsibilities for those involved in these reviews, and develop policies and schedules for their completion.

- There are Interim Standards for the classification and assessment of individuals to CBO homes. Additional work is needed to ensure the requirements pertaining to individual program plans and monitoring are met.

AUDIT SCOPE

6.9 In September 1997 we began an audit of certain aspects of the operation of long-term care facilities regulated by the Departments of Community Services and Health. The areas to be audited included licensing and inspection of these facilities, as well as classification and assessment of residents entering these homes. However, we separated the audit into two phases and are only reporting on the results of our audit of the classification and assessment function this year. The second phase of the audit will be reported in the 1998 Report of the Auditor General.

6.10 *Phase 1* - The objectives for Phase 1 of the audit were to assess the processes for classifying residents to homes based on their care needs, and for determining the level of assistance to be provided based on their financial need.

6.11 General criteria were used to facilitate Phase 1 of our audit. Criteria are defined as reasonable and attainable standards of performance and control against which the adequacy of systems and practices can be assessed. The following criteria were discussed with management at the beginning of the audit.

- There should be clearly defined policies and procedures for the classification and assessment processes and they should be consistent with the Social Assistance Act and regulations. Roles and responsibilities for these functions should also be clearly defined.

- The classification process should ensure that less costly alternatives which fully meet the applicant's needs are considered. The assessment process should include a review and verification of applicants' financial information, and there should be policies regarding those assets to be considered in determining financial need.

- Where an applicant's residence is designated under Section 8 of the Social Assistance Act, there should be a clear policy on entitlement to any rental income and disposition of proceeds in situations where a designated residence is sold.

- There should be periodic reclassifications and reassessments of residents to determine if care and financial needs should be adjusted.

6.12 Our audit approach consisted of interviews with management and staff at Community Services and Health. We performed detailed testing on the classification and assessment of homes for special care residents in two municipalities: Halifax Regional Municipality and Cape Breton Regional Municipality. Any findings and observations resulting from our testing with regard to homes for special care in these municipalities, where the initial review of care needs and financial circumstances is performed by Provincial caseworkers, may not extend to practices in other municipalities throughout the Province where caseworkers are employed by the municipalities, or where Community Services performs the work on behalf of the municipality.

6.13 *Phase 2* - The objectives of Phase 2 will be to assess:

- the licensing and inspection functions for long-term care facilities, including follow-up on deficiencies and enforcement of penalties;
- the processes for reviewing budgets and setting per diems;
- the processes for monitoring financial performance of facilities and compliance with government standards;
- the process for payment of claims received from facilities; and
- the planning functions related to demand and capacity, and the process for approval of new facilities or additional beds.

6.14 In addition, we intend to examine the Departments' plans and progress relating to establishing outcome measures for the Programs. Finally we will follow-up on the implementation of recommendations from our previous audit of Hospitals-Homes for Special Care Shared Services, reported in the 1992 Report of the Auditor General.

PRINCIPAL FINDINGS

Roles and Responsibilities

6.15 The assessment function involves obtaining financial data and other information from the applicant, and determining the level of financial assistance to be provided. The purpose of the classification process is to determine the level of care required by the applicant. Caseworkers make a recommendation as to the appropriate type of facility based on their review of information pertaining to the applicant's care needs. Based on this information, classifications and assessments are made by Community Support Specialists or Long-Term Care Advisors. The caseworkers use the classifications to help applicants find an appropriate home for special care. The roles and responsibilities for individuals involved in these processes are detailed in Exhibit 6.1.

6.16 The classification process for publicly-funded individuals applying to a nursing home or home for the aged was previously performed by Community Support Specialists at the Department of Community Services. Organizational changes resulted in this function being performed by Long-Term Care Advisors from the Department of Health. The Classifications and Assessments Manual notes classification and assessment as the responsibility of the Department of Community Services, but does not describe the role of the Long-Term Care Advisors at the Department of Health in classifying applicants who are likely to enter a nursing home or home for the aged. The Manual should be expanded to include the role of these Advisors.

Assessment of Financial Need

6.17 *Initial assessment* - The assessment process requires that the caseworker complete a Social Service Report, or Form B (see Exhibits 6.1 and 6.2). Among the sections to be completed is one noting financial information with respect to the applicant, including sources and amounts of the individual's monthly income and that of a spouse, if applicable. There is also a requirement to note the amount and type of assets owned by the applicant at the time of application, and whether this information has been verified. The caseworker concludes on the form whether the individual will be a private-paying or publicly-supported resident. We noted from our discussions that financial assessments are more relevant to applicants to nursing homes and homes for the aged. Assessments done for applicants to homes for which Community Services is responsible rarely indicate significant income or assets to aid in the cost of care.

6.18 There are Provincial policies regarding the amount and type of assets that can be retained by individuals or their families upon entry of an individual to a home for special care. However, our discussions with staff indicated that verification of income and assets varies throughout the Province, with some caseworkers doing very little work in this area and others obtaining detailed bank records, copies of income tax returns, etc. Current practices are a combination of practices that have developed over time, policies in draft manuals and policies from old municipal manuals. We tested files in Halifax Regional Municipality and Cape Breton Regional Municipality to determine the extent of financial verification. About one-half of files tested contained no evidence that financial information had been verified. Several files related to individuals in receipt of family benefits. We were informed financial data related to these residents is agreed to documentation on file in the family benefits system, but there is no indication in the files that this verification has taken place. Health and Community Services plan to establish a staff committee to address issues relating to financial assessments.

6.19 As part of the assessment process, caseworkers must determine whether there are more cost-effective alternatives to a home for special care that could meet the applicant's needs. We noted that these alternatives were considered in the vast majority of the files we tested.

6.20 The need for standard procedures for verification of assets and income of individuals receiving assistance from the Province is not unique to those applying for admission to long-term care facilities. Income levels for those registered under the Seniors' Pharmacare Program, for example, are verified against electronic files obtained from Revenue Canada. A similar procedure should be developed to verify the income of individuals who apply to be publicly-supported residents in homes for special care.

6.21 Possible financial contribution from relatives is also considered in the assessment of financial need. The Social Assistance Act provides that relatives defined in the Act are "*... jointly and severally liable for the assistance of the person* [receiving assistance] *and shall assist and maintain the person to the extent and in such manner as the social services committee may direct.*" Again, practices vary with respect to determining whether financial contributions from relatives are possible. It was indicated that contributions in kind, such as donations of clothing and personal supplies, are considered in some cases. We recommend that policies and procedures be developed in this area.

6.22 *Reassessment* - Finally, we determined that there are no requirements for periodic reassessment of a resident's financial situation. Caseworkers noted that they rely on staff at each facility to inform them if they become aware of changes in a resident's financial situation, but there is no formal requirement for the homes to do this. We recommend that roles and responsibilities be clarified with respect to the reassessment process and that policies require regular review of financial data.

6.23 We tested files of residents in Halifax Regional Municipality and Cape Breton Regional Municipality who had been admitted more than 36 months prior to the start of our audit to determine whether any periodic review of financial circumstances had been performed. We observed that only 23% had been reviewed to determine if their financial situation had changed since their original classification.

Classification to Level of Care

6.24 *Initial classification* - Individuals are classified to the level of care they require. The levels of care to which the Homes For Special Care Act applies are identified as Type I Care and Type II Care, with Type I Care being the less intensive level of care. We observed that classification levels are standardized and the distinction between Type I and Type II care is clear.

6.25 As noted in Exhibit 6.1, Community Support Specialists and Long-Term Care Advisors approve Form C for all publicly-supported applicants entering a home for special care. All but one of the files tested in Halifax Regional Municipality and Cape Breton Regional Municipality had a completed Form C on file. Individuals who pay per diem rates themselves may also be classified prior to entry to a home for special care. This is a requirement for applicants to municipally-owned homes and for applicants to any home located in the Cape Breton Regional Municipality. There is no formal requirement for this in other situations. We did not test to ensure that private-paying residents had been classified or that the classification had been approved.

6.26 *Classification review* - The Classifications and Assessments Manual notes that a review of the care needs of residents in nursing homes and homes for the aged must be performed twice a year, and annually for residents in residential care facilities.

6.27 For nursing homes and homes for the aged, classification reviews are now the responsibility of caseworkers. Prior to the Department of Health assuming responsibility for these homes, the reviews were conducted by Public Health Nurses. Due to the volume of clients of each caseworker, there is no time for regular reviews to reassess residents' care needs. There is a great deal of reliance on the home to notify the caseworker if a resident's condition changes, just as there is reliance with respect to reporting changes in a resident's financial situation. In addition, there are cases where a need for reclassification or review at some point in the future is noted by the caseworker or (less frequently) by the Long-Term Care Advisor. It is the responsibility of the caseworker to ensure these reviews are completed, but there is no system to track these reviews. We recommend that policies be developed to facilitate periodic reviews of care needs and to follow-up on residents where the need for a review or reclassification has been recommended.

6.28 For homes for which Community Services is responsible, classification reviews are the responsibility of Department staff who conduct the annual licensing inspection of homes. A review of the adequacy of level of care is to be conducted for each resident at the time of the licensing inspection. The reviews are documented with the licensing information gathered, and not in individual resident files. Since we have scheduled our audit of the licensing process for Phase 2 of our audit, we will follow up on this issue in next year's Annual Report.

Designated Residences

6.29 Section 8 of the Social Assistance Act defines a residence as a housing unit in the Province that has been inhabited by the applicant for at least two years. It further states that an applicant may designate this residence, and that the ownership of or interest in a designated residence shall not be taken into consideration when determining the level of social assistance to be provided to that individual. Designation means that the title to the residence may be transferred to another individual if the homes for special care resident wishes to do so.

6.30 This issue is more relevant to applicants to nursing homes and homes for the aged because applicants to homes for which the Department of Community Services is responsible rarely have a residence to designate. We discussed the issue of designated residences with management at the

Department of Health who indicated that if a resident chooses to sell his or her home, the treatment of sale proceeds varies across the Province. There are very few instances where, if a resident chooses to sell a designated residence, the proceeds are applied to the cost of care.

6.31 There is no discussion in the Act or its regulations of certain issues associated with designated residences. These include:

- the disposition of proceeds on sale by a resident, as noted above, or by another individual to whom title of the home has been transferred;
- the application of rental income from a designated residence toward the cost of care;
- guidelines as to the amount of land which may be included with the designated residence; and
- limits as to the value which may be designated.

6.32 The effect of Section 8 is to protect equity in a home from being used to pay per diems in a home for special care while equity in other forms of investment is not similarly protected. Consider that an individual may choose to invest savings in a residence or, alternatively, rent accommodation or live in someone else's home and use other types of investments. Section 8 results in a residence being treated very differently from other investments.

6.33 A policy, and perhaps changes in legislation, are needed to ensure consistent treatment of the proceeds on disposition of a designated residence. We also recommend that the legislation or policies be reviewed and expanded to address the issues noted above and other issues associated with designated residences.

Interim Standards for Community Based Options

6.34 Community Based Options are small long-term care facilities which are funded and administered by the various municipalities in Nova Scotia. On April 1, 1995 the Department of Community Services began to reimburse municipalities for all contributions made to publicly supported individuals residing in CBO homes. However, placements into the facilities were still done by both Provincial and municipal social workers. Effective April 1, 1998 Community Services will assume full responsibility for social assistance in the Province, and will be solely responsible for making such placements. Meanwhile, the government has developed interim standards for the placement of individuals and for the operation of CBO homes, while it explores how it will regulate the facilities when full responsibility is assumed.

6.35 The interim standards for Community Based Options require that individuals entering CBO homes be classified and assessed according to the procedures followed for homes for special care. As noted above, Community Support Specialists classify applicants to a level of care needed. CBO homes are not an option noted on the classification form (Form C), but the caseworker, perhaps in consultation with the Community Support Specialist, may decide to place an applicant in a CBO home if there is one available that meets the required level of care.

6.36 The interim standards require that individual program plans be developed for all residents, and that residents be monitored through caseworker meetings with service providers and quarterly reports from homes to the Department of Community Services. Our audit of CBO files indicated that these requirements are not being complied with in all cases. Fewer than half of the files we examined contained individual program plans, and fewer files showed evidence of ongoing monitoring. There were few quarterly reports from service providers on file.

6.37 We recognize that the interim standards were only one year old at the time of our audit and that time will be required to achieve full compliance. Staff have indicated that a review of the CBO program is presently ongoing and they plan to address these issues in the near future.

Policies and Procedures

6.38 The policies for classification and assessment are included in the Classifications and Assessments Manual developed by the Department of Community Services. It contains a description of the types of care available, and describes the procedures to be followed and forms to be used for classification and assessment. A list of these forms is noted in Exhibit 6.2.

6.39 During the course of our audit we noted inconsistencies in existing classification and assessment practices, or aspects of these functions where policies needed to be established. These were discussed in detail in the preceding paragraphs. The Manual should also be updated to promote consistency in policies and procedures throughout the Province and to establish new policies where needed.

6.40 There are draft policy manuals in Halifax Regional Municipality and Cape Breton Regional Municipality which describe caseworker practices unique to each of those municipalities. We were informed these practices result, in part, from policies and procedures developed by these municipalities when the initial review of care needs and financial circumstances was solely a municipal responsibility. Relevant policies and procedures from these draft manuals should be incorporated into the Manual revisions recommended above.

6.41 A Community Support for Adults Policy Committee has recently been established by the Departments of Community Services and Health. Its terms of reference include the review of policies and practices around the Province. We understand that this Committee will work on eliminating inconsistencies and developing Province-wide policies and procedures. Management at the Departments of Community Services and Health plan to have the more significant policy areas addressed by April 1, 1998 when all municipal involvement in the initial review of care needs and financial circumstances ends.

CONCLUDING REMARKS

6.42 Classification and assessment are based on a review of information provided by caseworkers. Significant work is needed to develop consistent policies across the Province to ensure that all applicants to homes for special care are classified and assessed in a consistent manner. In addition, procedures need to be established to ensure that financial information provided by applicants is verified. A system should also be established for the periodic review of care needs and financial status to ensure residents continue to be properly classified and that the level of financial assistance provided to them is appropriate.

6.43 Practices with respect to the type and amount of income and assets that can be retained by the applicant upon entry to a home for special care need to be made more consistent. More detailed policies are required for the designation of applicant residences.

6.44 The establishment of the joint committee, as described in paragraph 6.41, is a positive step towards implementing these recommendations and achieving consistent policies throughout Nova Scotia.

Exhibit 6.1

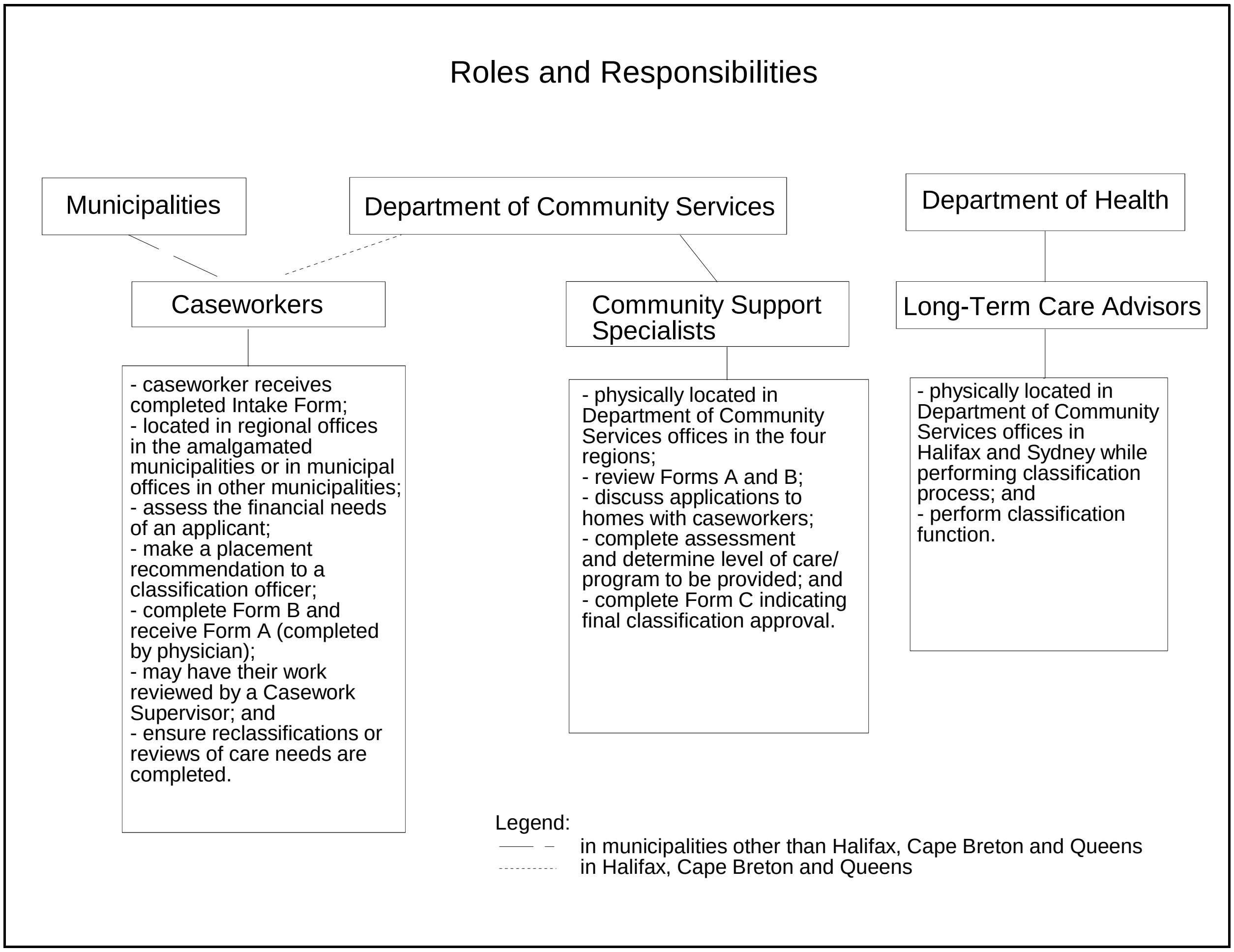


Exhibit 6.2

FORMS USED IN THE CLASSIFICATION AND ASSESSMENT PROCESS

Form A - Report of Applicant's Personal Physician

Form B - Social Service Report (key document in financial assessment process)

Form C - Approval to Admit a Person to a Home for Special Care (key document in classification process)

Others: Intake Form
Application for Social Assistance
Release of Information Consent Form

DEPARTMENT OF COMMUNITY SERVICES' RESPONSE

The Department of Community Services is pleased to receive the timely and supportive feedback from the Office of the Auditor General on The Homes for Special Care and Community Based Options Program; programs in the midst of a major review and redesign.

As noted in the Audit Report the Department of Community Services is in the process of the most comprehensive restructuring of social services in the province since the 1960's. On April 1, 1998, the Department of Community Services will assume responsibility for the delivery of all social services, which will include the assessment, classification and case management of all publicly supported individuals requiring residential care and programming. In preparation for this total transfer, activities within the Homes for Special Care and Community Based Options Program have been concentrated on the development of a provincial policy and standards with regard to classification and placement of individuals and the development of a provincial case management policy and standards to monitor individuals following placement.

This policy work will provide consistent application throughout the province of standards with regard to financial assessment, allowable assets, designation of residence, pre-admission and ongoing follow-up and review of program/care and finances post admission.

Concurrent activities underway within the Department of Community Services include a province-wide review of all Community Based Options as, effective April 1, 1995, the Department of Community Services assumed full financial responsibility for this municipal program and effective April 1, 1998 will, in addition to the financial responsibility, assume full program/case management responsibility. With the introduction of the Interim Standards Community Based Options Program in November 1996 the Department of Community Services provided a provincial standard under which this program would operate pending the completion of the review and the determination of a new framework for the continuum of long term care services in the province of Nova Scotia.

Over the past 18 months the Departments of Community Services and Health have been collaborating on the need for a continuum of long term care and services in Nova Scotia which will be based on a client-centred model, emphasizing ease of access in an efficient and cost-effective manner. Discussion/consultations will be ongoing with representatives of the long term care sector.

7.

ECONOMIC DEVELOPMENT AND TOURISM - TOURISM NOVA SCOTIA

BACKGROUND

7.1 The Economic Renewal Act, enacted in June 1994, assigns responsibility to the Minister of Economic Development and Tourism (ED&T) for matters relating to the economic renewal of the Province. The mandate of the Department defined in the Act includes the requirement to "*encourage and enhance the continued growth of tourism and tourism industries in the Province.*" The Act identifies Tourism Nova Scotia (TNS) as a possible division of the Department.

7.2 As noted in *Government By Design* (1996-97), one of the strategic goals of ED&T is to "*encourage a healthy and growing tourism industry"*. This document also identifies the *Value of the tourism sector* as one performance measure for government with regards to economic renewal. It notes the value for 1994-95 at $880 million with a target of $1 billion for the year 2000 and $1.25 billion for the year 2005.

7.3 As defined in the 1996-97 business plan of TNS, the mission of the division is to "*lead the growth and development of tourism as a key sector in the economic renewal of Nova Scotia by creating jobs, generating revenue and enhancing our quality of life.*"

7.4 The 1997-98 *Estimates* note that Tourism Nova Scotia supports its mission "*by encouraging a globally competitive tourism product and industry and by disseminating accurate and timely information*."

7.5 Tourism Nova Scotia's strategic business plan for 1996-97 notes that by supporting the development of the tourism product and industry, TNS "*delivers a high level of visitor satisfaction, helps to draw new visitors, extend stays and increase spending*". The strategic business plan also identifies seven goals towards achieving TNS's mission.

" - *to have the right products for the right markets*
- *to provide customers with quality tourist experiences of good value*
- *to market our products effectively*
- *to develop effective leadership and partnerships among industry stakeholders*
- *to foster a supportive business environment and an entrepreneurial customer-oriented business culture within the tourism sector*
- *to improve transportation access from key markets and to enhance transportation infrastructure within the province, and*
- *to nurture and protect our tourism assets"*

7.6 The 1996-97 actual net expenditures of the division were approximately $6.7 million. This represents 10% of the total net expenditures of ED&T. Exhibit 7.1 on page 67 shows a breakdown of gross and net expenditures by classification. It also shows expenditures by program area as defined in the *Estimates*. The 1997-98 estimated net expenditures of the division are $7.4 million.

7.7 As of November 1997 there were 187 staff positions for Tourism Nova Scotia. Exhibit 7.2 on page 68 shows the breakdown of the positions, by type, for the division and the resort hotels for which TNS is responsible. TNS represents 22.3% of the staff of the Department. If the hotel staff are also included, this percentage increases to 73.3%.

7.8 The Tourism Nova Scotia publication *1996 Nova Scotia Tourism Statistical Review* notes,

> *"Tourism, a major force in both the national and provincial economies, generates hundreds of millions of dollars in sales for Nova Scotia businesses, and tens of thousands of jobs for Nova Scotia workers. In addition, both the provincial government and municipal governments receive tens of millions of dollars in tax revenues from tourism related expenditures and business every year. These benefits are realized in virtually every area of the province and span a range of industries almost as broad as the economy itself."*

7.9 Tourism Nova Scotia and the Nova Scotia tourism industry reported in a press release in November 1997 that "*1997 tourism receipts will exceed $1 billion dollars.*" This exceeds the target for the 1999-2000 fiscal year noted in *Government By Design*. Exhibits 7.4 to 7.8 have been included on pages 69 to 71 to provide information on the tourism industry in Nova Scotia. A majority of the information for these Exhibits has been extracted from *Strategy for Nova Scotia* and *1996 Nova Scotia Statistical Review*, which were produced by, or with input from, TNS. These Exhibits refer to tourist seasons so for example 1996 means the 1996 tourist season which occurred during the 1996-97 fiscal year. This would apply to the remainder of the report as well. The exhibits include the following information.

- Exhibit 7.4 - Historical analysis of tourism employment from 1994 - 1997.
- Exhibit 7.5 - Historical analysis of number of person visits from 1994 - 1997.
- Exhibit 7.6 - Analysis of visitors by region of origin for 1996.
- Exhibit 7.7 - Historical analysis of tourism receipts from 1994 - 1997.
- Exhibit 7.8 - Analysis of tourism receipts by business sector for 1996.

7.10 During the fall of 1997 we conducted a review of certain aspects of Tourism Nova Scotia. The purpose of this chapter is to provide summary information on the operations and activities of Tourism Nova Scotia.

RESULTS IN BRIEF

7.11 The following are the principal observations from our review.

- Tourism Nova Scotia is working closely with stakeholders to ensure growth in the tourism industry including the development of plans. The development of a Tourism Partnership Council to be operational in 1998-99 will change the way tourism is managed in the Province. There will be more involvement by industry in planning and delivering services related to tourism, with the Council being accountable to government and industry.

- Improvements are required in the information reported to the House of Assembly on the operations of Tourism Nova Scotia. Tourism Nova Scotia creates publications for industry and the public including information on operating results in the tourism industry which could support the preparation of an annual report. ED&T has not produced an annual report even though one is required by legislation.

- Tourism Nova Scotia uses outcome measures to monitor the achievement of the mission of the division. During our review we noted opportunity for improvement in the reporting on outcome measures.

- Tourism Nova Scotia has established processes to ensure compliance with the Tourist Accommodations Act and regulations, and the division is complying with the *Government Procurement Policy*.

- Tourism Nova Scotia entered an agreement with CorporaTel effective May 1, 1994 for the management of a computerized information and reservation system owned by the Province (Check In). Tourism Nova Scotia has received adequate information to monitor the performance of CorporaTel and compliance with the Agreement. This information has included a review performed by external consultants. At the time of our review, Tourism Nova Scotia was undecided as to whether another review would be completed by consultants. The receipt of independent information is required to adequately monitor compliance and performance of CorporaTel with regard to the Agreement. This could be performed by consultants or staff of ED&T.

SCOPE OF REVIEW

7.12 The objectives of this assignment were to obtain background information on the operations of Tourism Nova Scotia and review selected aspects of its operations including processes in place to ensure due regard for economy and efficiency and compliance with applicable legislation and the *Government Procurement Policy*.

7.13 Our approach included interviews with management and staff of Tourism Nova Scotia and the Nova Scotia Marketing Agency as well as a review of legislation and information made available to us.

7.14 Our review of compliance with the *Government Procurement Policy* was limited to a selected sample of expenditures recorded in the 1996-97 fiscal year. The initial procurement decision on these transactions may have been made prior to that time.

PRINCIPAL FINDINGS

7.15 Information and observations on Tourism Nova Scotia resulting from our review are discussed under the following headings.

- Follow-up to 1993 Management Audit
- Organization
- Planning
- Accountability
- Interactions
- Compliance
- Quality Assurance
- CorporaTel Agreement

Follow-up to 1993 Management Audit

7.16 In 1993, the Nova Scotia government commissioned a series of management audits of departments with the objective of identifying opportunities for efficiency improvement and better program delivery. At the same time, the government announced that the Departments of Tourism and Culture, and Economic Development would be merged. The report of the combined management audit of these two departments was released in November 1993. It identified a number of opportunities for improvements to be considered when creating the Nova Scotia Economic Renewal Agency (now the Department of Economic Development and Tourism) which was established in June 1994 through the Economic Renewal Act.

7.17 The management audit report suggested a timeframe of three years to implement or address all the recommendations. In 1994-95 we met with senior management of the Department to obtain an overview of how they had or were dealing with the matters reported. We reported the results of our enquiries in Chapter 16 of our 1994 Report.

7.18 During this year's assignment we followed up on the progress made in addressing the recommendations of the management audit which related specifically to Tourism Nova Scotia. Exhibit 7.9 on page 72 provides the Departmental responses to these recommendations.

Organization

7.19 Exhibit 7.10 on page 74 shows the overall governance, accountability and management organization of TNS. The Director of Community Relations and the Controller are support positions for the Division.

7.20 Exhibit 7.1 on page 67 shows the actual 1996-97 expenditures of Tourism Nova Scotia by functional area. TNS administers seven grant programs. The total advanced under these grant programs in 1996-97 was approximately $1.4 million. Exhibit 7.3 describes three of the larger grant programs which represent approximately 70% of total grant payments made in 1996-97.

7.21 Tourism Nova Scotia is divided into four functional areas: Tourism Development; Quality Services; Field Services; and Enquiry and Research Services.

7.22 Tourism Development is responsible for coordinating the planning and implementation of strategies to develop the tourism product and industry. It develops policies to support growth and development of the tourism industry.

7.23 Quality Services is responsible for ensuring quality service and product delivery. Its responsibilities include:

- administering the Tourist Accommodations Act and regulations including inspection services, (see paragraph 7.56);
- administering the Award of Quality Programs of TNS (paragraph 7.56); and
- the operations of the three Provincial resort hotels.

7.24 The net expenditures for the hotels are not included in those reported for TNS. They are reported by ED&T as a separate budget subject. For 1996-97 the resort hotels recorded an operating profit of approximately $176,000. However, this figure does not include all Provincial costs of operating the hotels, such as the capital and maintenance costs incurred by the Department of Transportation and Public Works. Exhibit 7.14 is a copy of the unaudited financial information included in Volume II of the March 31, 1997 *Public Accounts*.

7.25 Field Services is responsible for the operation of the 15 Provincial visitor information centres (VICs) as well as the visitor services at Peggy's Cove. Eight of the centres are located throughout the Province, one is located in each of Prince Edward Island and Maine, and five are located on ferries travelling to Nova Scotia from various locations. These centres provide a range of services to tourists including information counselling by staff, and the distribution of tourism literature. Some locations have access to the Provincial information and reservation system. This system is the responsibility of Enquiry and Research Services.

7.26 Enquiry and Research Services (E&RS) is responsible for the Provincial information and reservation system (Check In) which is discussed in more detail in paragraph 7.57. E&RS manages the distribution centre which distributes tourism literature throughout the VICs and fulfills consumer requests for tourism literature which are received through Check In. E&RS is also responsible for gathering and analyzing data to provide information and statistics to support decision making within Tourism Nova Scotia and the tourism industry.

Planning

7.27 *Strategic* - For 1997-98 there are three planning documents which have been developed to manage tourism in the Province. The documents are:

- Strategy for Tourism;
- 1997-98 Tourism Marketing Plan; and
- Tourism Nova Scotia Strategic Business Plan for 1997-98.

7.28 The Strategy for Tourism was published in March 1996 and covers the next five years to 2001. It provides the vision of tourism in the Province along with the key goals, strategies and actions to achieve this vision. It was developed by a committee with representation from TNS; the Tourism Industry Association of Nova Scotia (TIANS); the Atlantic Canada Opportunities Agency; Voluntary Planning (which is an organization of non-government individuals whose operations are funded by ED&T); and the Nova Scotia Marketing Agency (NSMA) - a division of ED&T.

7.29 An Implementation Committee with representation from industry and government was established to facilitate implementation. A number of initiatives have been identified which address a majority of the actions required by the Strategy. The Committee developed an action status document which identifies actions, the responsible government and industry leaders and partners and the timing of activities. The Committee uses this document to monitor progress.

7.30 The 1997-98 Tourism Marketing Plan was completed by the Nova Scotia Marketing Agency. It identifies measurable marketing objectives and activities required to support the goals of TNS. However, there is no clear linkage to the goals of TNS. This has been recognized by TNS and the NSMA, and has been addressed in the 1998-99 tourism marketing plan.

7.31 The Tourism Nova Scotia Strategic Business Plan for 1997-98 identifies the vision, mission and goals for Tourism Nova Scotia consistent with the Strategy for Tourism. The business plan also identifies the priorities for 1997-98 required to achieve these goals. These priorities are linked to the strategic goals of ED&T.

7.32 *Financial* - TNS prepares an annual budget which is reviewed and challenged at a meeting of senior management of ED&T, and incorporated in the Department's budget included in the annual *Estimates*.

Accountability

7.33 *Roles and responsibilities* - The roles and responsibilities of Tourism Nova Scotia are defined in the Economic Renewal Act, and the various planning documents related to tourism in the Province.

7.34 The responsibilities of the Executive Director of TNS, along with the staff reporting to him, are described in job descriptions. The approved job descriptions of the staff are not current.

7.35 Performance evaluations of staff reporting to the Executive Director have not been completed by the current Executive Director because of his recent appointment. The Executive Director plans to complete these in the near future.

7.36 *External reporting* - There is no specific reporting to the House of Assembly on the operations of TNS other than the estimated expenditures included in ED&T's annual budget submission and the total actual expenditures compared to budget which is reported in the *Public Accounts*. Annual reporting to the House of Assembly, by ED&T, is required by the Economic Renewal Act, however this has not occurred. The Deputy Minister has indicated that a detailed report for 1997-98 will be completed with summary reports prepared for prior years.

7.37 Tourism Nova Scotia prepares two reports for the tourism industry and the public on some of the operating results in the tourism industry. *Tourism Insights* is published monthly and *Tourism Industry Facts* is published annually. Exhibits 7.4 to 7.8 on pages 69 to 71 include extracts from these publications. This type of information could be included in an annual report.

7.38 The publication *Nova Scotia Counts*, to be released in 1997-98, will report on the accomplishments of departments, including ED&T, against the business plans of the departments described in *Government By Design*. (See Chapter 2, page 14)

7.39 *Internal reporting* - There are no defined reporting requirements to senior management other than financial actual to budget comparisons. However, there are daily, weekly and monthly reports on various topics provided to senior management. These include information on inspection reports completed, resort operations, visitation activity at the VICs and distribution centre activities.

7.40 Within the division, weekly status meetings are held with staff reporting on the various plans and projects within TNS.

7.41 *Outcome measures* - TNS recognizes the importance of outcome measures in monitoring the performance of the division. TNS gathers information and reports on a number of outcome measures, through *Tourism Insights* and *Tourism Industry Facts*. These measures demonstrate the economic impact of tourism in the Province and relate to the achievement of the mission of the division. However, at the time of our review, improvements in reporting could have been made by reporting the outcome measures of the division in a way that tied them to the seven goals of TNS, listed in paragraph 7.5, to demonstrate the division's progress in achieving each goal. Further, outcome measures had yet to be defined for all of the division's goals.

7.42 As noted in paragraph 7.43, there is a need for TNS and the NSMA to work closely together. According to senior management of TNS and the NSMA, the two divisions are planning to develop combined outcome measures appropriate for both divisions.

Interactions

7.43 *Internal* - The plans and activities of TNS and the Nova Scotia Marketing Agency have a direct impact on each other. It is important that they work closely and cooperate to ensure success in achieving their objectives.

7.44 The NSMA was involved in developing the *Strategy for Tourism* and TNS was involved in developing the *1998-99 Tourism Marketing Plan*.

7.45 The Executive Director of TNS is involved in weekly status meetings of the NSMA where NSMA staff report on various plans and projects related to tourism marketing. Over the past year, the Executive Director of TNS and the NSMA were also involved in bi-monthly meetings of all divisional management of ED&T to deal with policy and operational issues related to tourism.

7.46 In addition, weekly meetings of senior management of ED&T ensure all are aware of the activities and plans of the other divisions within ED&T.

7.47 *External* - There are a number of stakeholders involved in the tourism industry. Tourism Nova Scotia interacts with departments of both the Provincial and Federal government as well as government agencies, and industry groups and associations. Exhibit 7.11 includes a list of some of those stakeholders.

7.48 There has been an effort to involve members of the tourism industry in identifying and achieving actions required to develop tourism in the Province. A number of government-industry committees have been created which reflect the efforts of government to work in partnership with industry in addressing the needs of the Province. The committees created include:

- Tourism Strategy Implementation Committee (paragraph 7.29);
- Tourism Marketing Alliance;
- Tourism Partnership Planning Committee; and
- Tourism Marketing Strategy Group.

7.49 The Tourism Marketing Alliance was established to collect industry feedback on the 1997-98 tourism marketing plan developed by the NSMA.

7.50 The Tourism Partnership Planning Committee was created in January 1997. It will dissolve once the Tourism Partnership Council, discussed in paragraph 7.51, is formed. The Committee was established to identify a partnership structure between government and industry to manage tourism and ensure growth in the industry. In a slide presentation concerning the Tourism Partnership Council the following was noted. "W*e have seen the value of tourism grow over the past several years. In Canada, there has been an average increase of 24% since 1992. But in Nova Scotia, since 1992, our increase has been at the 16% level.*"

7.51 In the fall of 1997, a partnership model was taken to industry and government for consultation and was accepted, with modifications. As a result, at the time of our review, it was intended that a Tourism Partnership Council be created by the end of fiscal 1997-98. Its mandate is to include marketing tourism for the Province, assisting industry to prepare tourism products for the market, advising ED&T on how its other tourism programs impact on the Council's mandate and developing strong communications with industry and government.

7.52 At the time of our review, it had been determined that the Council would be made up of 16 members with 14 from industry. Government was to provide administrative funding while government and industry would cost-share programs on an individual basis. Programming would be based upon a jointly developed industry-government marketing strategy. Staff of ED&T would support the Council. The Council was to be accountable to government and industry and would produce an annual report.

7.53 The Tourism Marketing Strategy Group was created to provide for industry involvement in the development of the 1998-99 tourism marketing plan, and to begin work on developing a five-year strategic plan for marketing tourism in the Province. Once the Tourism Partnership Council becomes operational, it will take over the responsibilities of this Group.

Compliance

7.54 *Tourist Accommodations Act and Regulations* - The Tourist Accommodations Act and regulations require that all roofed tourist accommodations and camping establishments obtain an annual license from ED&T. They set the minimum quality standards for each type of establishment and provide for inspection. Processes and procedures have been established to ensure compliance with the requirements of the Act and regulations.

7.55 *Government Procurement Policy* - On January 1, 1996, the government released a *Policy on Government Procurement*. During this assignment we reviewed a sample of procurement transactions for compliance with the Policy. We found that the division was complying with the *Policy on Government Procurement*.

Quality Assurance

7.56 As noted above, one of the roles of Tourism Nova Scotia is to support the delivery of a high level of visitor satisfaction in order to draw new visitors, extend stays and increase visitor spending. Department staff have established some processes for evaluating the quality of service provided to tourists when they visit the Province. These processes include:

- *Inspections* - According to the Tourist Accommodations Act, *"an accommodation officer or campground accommodation officer may, at all reasonable times, enter and inspect any roofed accommodation or camping establishment or other building or premises in which accommodation for the travelling or vacationing public is provided or offered."* TNS has established a policy which requires that all fixed-roof accommodations and non-government camping establishments be inspected, on an annual basis, for compliance with the minimum standards of quality identified in the regulations to the Act. The Tourist Accommodations Act gives ED&T the authority to cancel or suspend an operating license if the standards of quality are not met and the authority to enforce the requirement of a license, in order to operate. According to staff, there have been no licenses cancelled or suspended in the past. However, problem properties will be removed from the Provincial Travel Guide. None were removed in the 1996 tourist season but nine were removed from the 1997 guide. In the 1996 tourist season there were approximately 900 fixed roof accommodations and 125 non-Provincial camping establishments.

- *Award of Quality Programs* - Award of Quality Programs were established for campgrounds in 1993-94 and VICs in 1994-95. Participation in the Award of

Quality Program for campgrounds is voluntary. The purpose of the program is to improve the service quality offered by campground operators. Qualifying campgrounds are accredited in the Provincial Travel Guide. The standards required for the Award of Quality accreditation are in excess of the minimum standards required by legislation. The purpose of the VIC program is to ensure a professional level of service is consistently provided and recognizable to visitors by the "Award of Quality" logo. Standards are established by TNS and all VICs are inspected annually. This includes the 15 provincial VICs and approximately 65 local VICs. For local VICs, Provincial funding for operations are contingent upon the VIC meeting the established minimum standards.

- *Feedback from Travel Guide* - At the back of the travel guide there is a questionnaire which tourists can complete concerning their experiences during their visit to the Province. TNS staff maintain a database of the comments received. According to staff any action taken on negative comments received would depend on the severity of the problem identified. The information gathered can have an impact on the timing of an inspection of an establishment as discussed above. An annual report is produced for internal use which summarizes the results of the compliments and complaints received. It is used to identify potential problems with regards to the quality of service provided to tourists.

CorporaTel Agreement

7.57 *Overview* - In 1978, the government, along with the Tourism Industry Association of Nova Scotia, initiated a toll-free, computerized information and reservation system. Through this system an individual can reserve accommodations or a car, and acquire detailed tourist information about the Province including such items as packaged tourist products offered. This system also provides the Province with a database of information it can use to plan and manage the tourist industry. This system was managed by Check Inns Limited, a crown corporation, until May 1 1994, when government entered a partnership agreement with CorporaTel for management of the system.

7.58 The Province owns the system software and CorporaTel is responsible for and has sole possession of the hardware for the duration of the Agreement. Upon completion of the Agreement, the hardware becomes the property of the Province. The Agreement ends on April 30, 1999. There is an option to renew the Agreement for three years but no decision has yet been made as to whether the Province will exercise that option.

7.59 Membership in the information and reservation system includes fixed-roof tourist accommodations, campgrounds, and car rental companies. The system represents over 90 % of the total rooms available in Nova Scotia. It also represents some entities outside the Province. Exhibit 7.12 on page 76 provides a description of the membership numbers based on the 1997 season travel guide. The information and reservation system answered 373,334 inquiries, made 57,559 reservations and distributed 273,300 pieces of tourist information.

7.60 *Expenses and revenues* - Through the Agreement, the Province pays certain expenses to CorporaTel for the operation of the information and reservation system. A majority of the payments relate to a per minute charge on all calls received. The Province also pays for long-distance charges on calls, the cost of certain mailing labels and some hardware and software costs which were incurred at the beginning of the Agreement.

7.61 CorporaTel collects commission revenue on behalf of the Province for sales made by members through the system. Since the Province owns the software, they are also entitled to a $15,000 royalty for each sale of the software by CorporaTel. Since the beginning of the Agreement, CorporaTel has sold the software to three others but have only paid the Province $15,000 for the first sale. The last two sales were made in 1996-97 . TNS is pursuing receipt of the remaining $30,000.

7.62 Exhibit 7.13 on page 76 details the expenses and revenues from the beginning of the Agreement to March 31, 1997.

7.63 There are processes in place to ensure the Province is receiving all revenue to which it is entitled. As well, there is a clause in the Agreement which allows the *Province's auditor* access to CorporaTel's records in relation to the Agreement. In the 1994-95 fiscal year, the first year of the Agreement, ED&T internal audit conducted an audit and reported that *"the systems in place at CorporaTel to record and control the financial aspects of the contract are adequate and the information available is more than sufficient to support the commissions due or the billings to the Province."* At the time of our review, internal audit was planning to conduct a similar audit at CorporaTel before the end of fiscal 1997-98.

7.64 *Monitoring compliance and performance with the Agreement* - Performance standards are identified in the Agreement and CorporaTel provides information on performance against those standards. One performance standard which was not identified was customer satisfaction level.

7.65 At this time, TNS is receiving adequate information to ensure CorporaTel is complying with its requirements according to the Agreement and to measure performance. TNS hired a consultant to review and report on the performance of CorporaTel in providing the services required. The review covered such areas as telephone response times, literature request fulfilment time, and overall service experience such as friendliness and knowledge of information requested. Without this review, the division would have had to rely on information provided by CorporaTel in order to monitor the Agreement. This study covered a period of 12 months beginning in May 1996 with nine months chosen for testing during that period. According to staff, the contract was extended with testing being done to the fall of 1997. Staff have yet to determine whether another review will be conducted.

7.66 *Economy of the CorporaTel Agreement* - According to staff of TNS the cost per call is lower now than it was when Check Inns Limited was running the information and reservation system. This was one area that internal audit intended to include in a review of the Agreement in 1997-98, and should be included in order to conclude upon the economy and efficiency of the arrangement.

CONCLUDING REMARKS

7.67 Tourism is a significant contributor to the economy of the Province. Tourism Nova Scotia has demonstrated a commitment to supporting the development and growth of tourism in the Province. For the past few years Tourism Nova Scotia has worked with key stakeholders to develop strategic and operational plans to ensure success. The development of a Tourism Partnership Council, to be operational in 1998-99, will change the way tourism is managed in the Province, including stronger involvement of industry. With this change, there will be new challenges to address such as ensuring an appropriate accountability framework for the Council.

7.68 One objective of this assignment was to provide information to the House of Assembly on the operations of Tourism Nova Scotia. Improvements in the flow of information are required and could be achieved by tabling an annual report for the Department of Economic Development and Tourism, including Tourism Nova Scotia, as required by legislation.

Exhibit 7.1

ANALYSIS OF EXPENDITURES
MARCH 31, 1997
(Source: Department of Finance general ledger and staff of ED&T)

Expenditure Classification	Net Expenditures Per General Ledger	Gross Expenditures	% of Total Gross Expenditures
Salaries and benefits	$ 1,853,573	$ 1,853,573	25.1
General operating supplies	1,795,703	2,260,143	30.5
Grants	1,445,023	1,445,023	19.5
Other	1,591,141	1,840,761	24.9
Total	$ 6,685,440	$ 7,399,500	100.0

Program Area	Gross Expenditures	% of Total GrossExpenditures
Check In Information/Reservation System	$ 2,104,351	28.4
Visitor Information Centres (VIC)	897,832	12.1
Distribution Centre - Distributes tourism literature to VIC and as requested through Check Ins	673,583	9.1
Bluenose II- Grant and other expenses to operate the vessel	514,996	7.0
Other program areas (less than $500,000)	3,208,738	43.4
Total	$ 7,399,500	100.0

Functional Area	Gross Expenditures	% of Total Gross Expenditures
Tourism Development	$ 1,308,790	17.7
Quality Services	434,669	5.9
Enquiry and Research	3,255,387	44.0
Field Services	1,392,815	18.8
Support Services	1,007,839	13.6
Total	$ 7,399,500	100.0

Exhibit 7.2

ANALYSIS OF JOB POSITIONS COMPARED TO THE DEPARTMENT NOVEMBER 1997 (Source: Staff of ED&T)

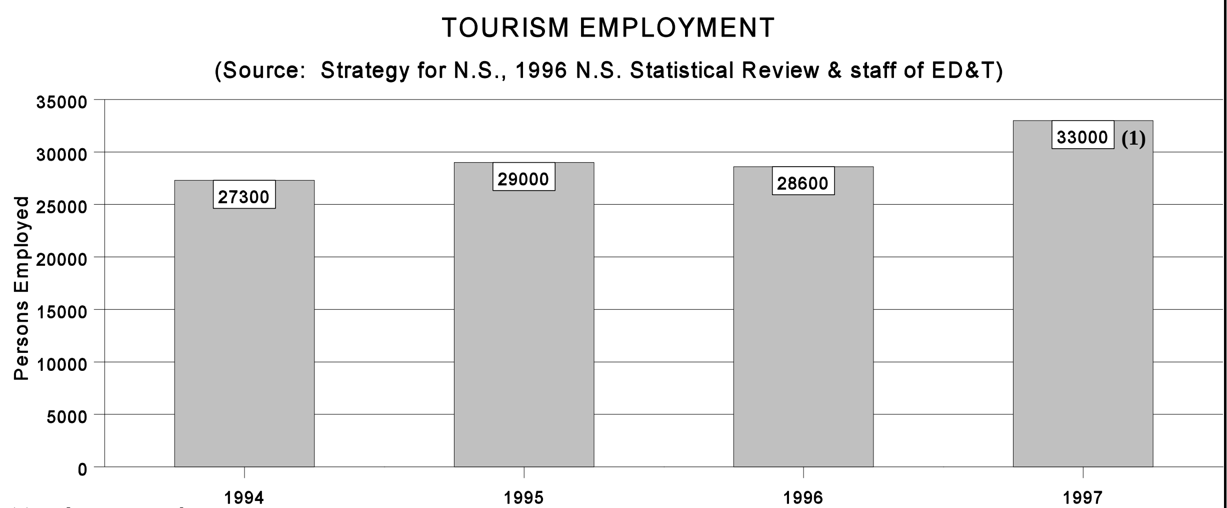
Position	Tourism Division	Resort Hotels	Total ED&T
Full Time Employees	32	18	234
Casual/Term Employees	21	5	55
Contract Employees	2	6	19
Seasonal Employees	132	400	532
Total	187	429	840

Exhibit 7.3

GRANT PROGRAMS ADMINISTERED

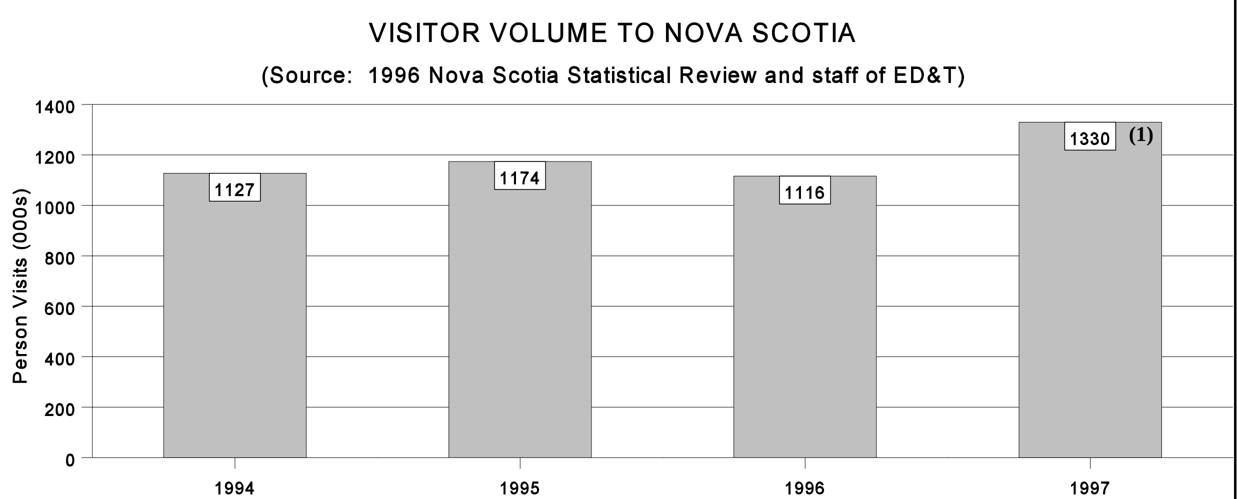
Functional Area	Grant Program	Program Purpose	1996-97 Expenditures
Tourism Development	Development Projects	To fund projects which help develop the market, contribute to the development of destinations and travel generators, and contribute to the enhancement of our scenic travelway system	$ 383,596
	Regional Association Support	To support the Regional Tourist Associations so they can operate the local VICs. The funds are used for staffing the VICs, etc.	218,269
Support Services	Bluenose II	To operate the vessel.	406,482
Other			436,676
Total			$ 1,445,023

Exhibit 7.4



(1) Preliminary number

Exhibit 7.5



(1) Preliminary number

Exhibit 7.6

**VISITATION TO NOVA SCOTIA
BY REGION OF ORIGIN, 1996 TOURIST SEASON
(Source: 1996 Nova Scotia Statistical Review)**

Region	% of Total Visitations
Atlantic Canada	48%
Ontario	22
Other areas of the United States	12
New England, United States	8
Quebec	5
Western Canada	3
Overseas	2
	100%

Exhibit 7.7

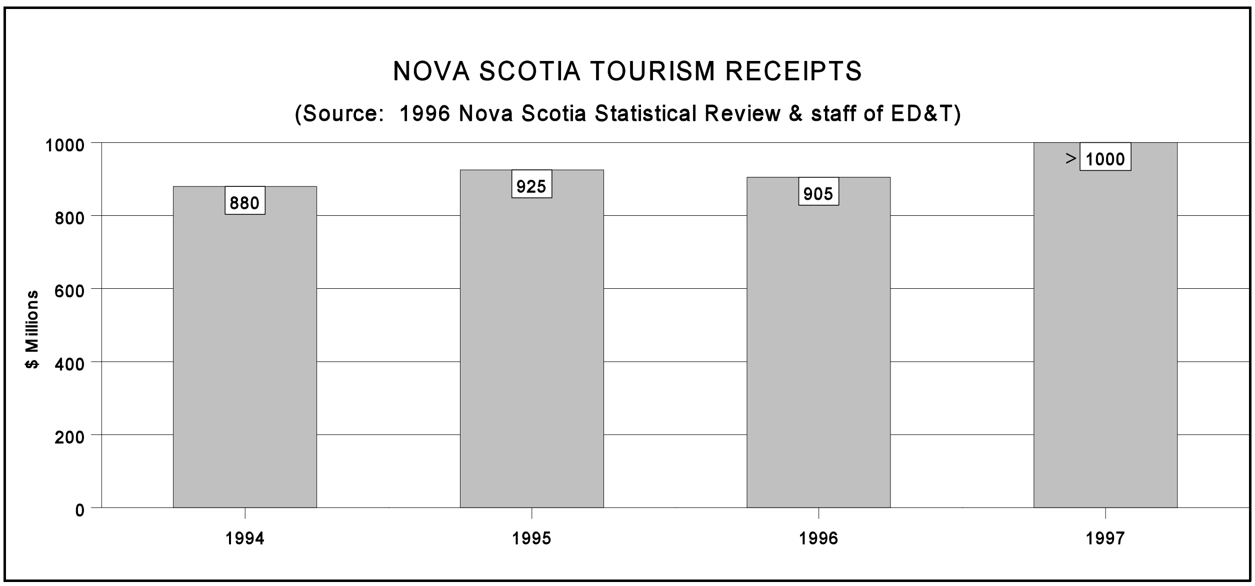


Exhibit 7.8

ANALYSIS OF TOURISM RECEIPTS
1996 TOURIST SEASON
(Source: 1996 Nova Scotia Statistical Review)

Business Sector	% of Tourism Receipts
Transportation	20%
Restaurants	18
Shopping	17
Fixed-Roof Accommodations	15
Automobile and Fuel	14
Groceries and Liquor	6
Entertainment	5
Other	5
	100%

Exhibit 7.9

FOLLOW-UP TO THE 1993 MANAGEMENT AUDIT RECOMMENDATIONS STATUS AS OF NOVEMBER 1997

Recommendations	Department Comment
1. Divisions currently operating within Tourism and Culture consolidate their grant programs into a smaller number of well-defined and flexible programs.	Cultural Affairs Division grant program was transferred to Department of Education and Culture.
2. Explore the potential for amalgamation or consolidation of provincial and locally operated visitor information centres (VIC) and establishing a Visitor Information Centre Commission with costs and benefits clearly documented.	A draft contract has been forwarded to Tourism Cape Breton to manage Port Hastings VIC on behalf of the Province in 1998. Partnership with Halifax Regional Municipality for downtown Halifax VIC continues. Antigonish VIC turned over to Antigonish Eastern Shore Tourist Association, decreasing transitional funding provided.
3. Explore options to reduce the cost of literature distribution including privatization of literature fulfilment and cost recovery through charging private operators for distribution of their literature.	The Nova Scotia Marketing Agency and Tourism Nova Scotia are participating in a broader initiative involving other government departments at the urging of Transportation & Public Works.
4. While generally supporting the notion of privatizing Check Inns, the option of an Atlantic-wide system should be revisited.	Other provinces are not prepared to commit financially to an Atlantic-wide system, however privatization of Check Inns was completed.
5. Explore the possibility of privatizing or out-sourcing property inspections.	Canada Select is currently inspecting member properties (300) for Tourism Nova Scotia with the exception of new and problem accounts. TNS is considering tendering for all fixed roof inspections for 1998.
6. Architectural design work should be left to the private sector.	The department architect retired in 1996. Since then there has been very little large scale construction that would require an architect. Any work to be done has been handled by Department of Transportation and Public Works. We have a good relationship with them and they have qualified staff.
7. Assistance provided to the private sector operators in the form of business plans and financial restructuring plans, which is currently provided free of charge, should be left to the private sector.	Assistance is no longer provided to the private sector for business plans.

Recommendations	Department Comment
8. Management of the three provincial resorts be contracted out to the private sector using operating leases.	A request for proposal was issued, an operator selected against criteria and a contract negotiated. It was rejected by Executive Council. The direction of the three resorts is now under the Quality Services Section of Tourism Nova Scotia. There is a proposal being drafted to recommend the resorts be set up as crown corporations.
9. Should the Bluenose II continue to operate as a working vessel and if a new vessel is required, funding should be by the private sector.	The Bluenose II Preservation Trust is operator of the vessel under contract with ED&T. Daily operations are funded by private donations and a grant from the Province. The refit was funded by private donations and through a cooperation agreement. It is more cost efficient to operate the Bluenose II in this manner. When the cost of operations was paid by the taxpayers of the Province, costs were in the range of $1 million.

Exhibit 7.10

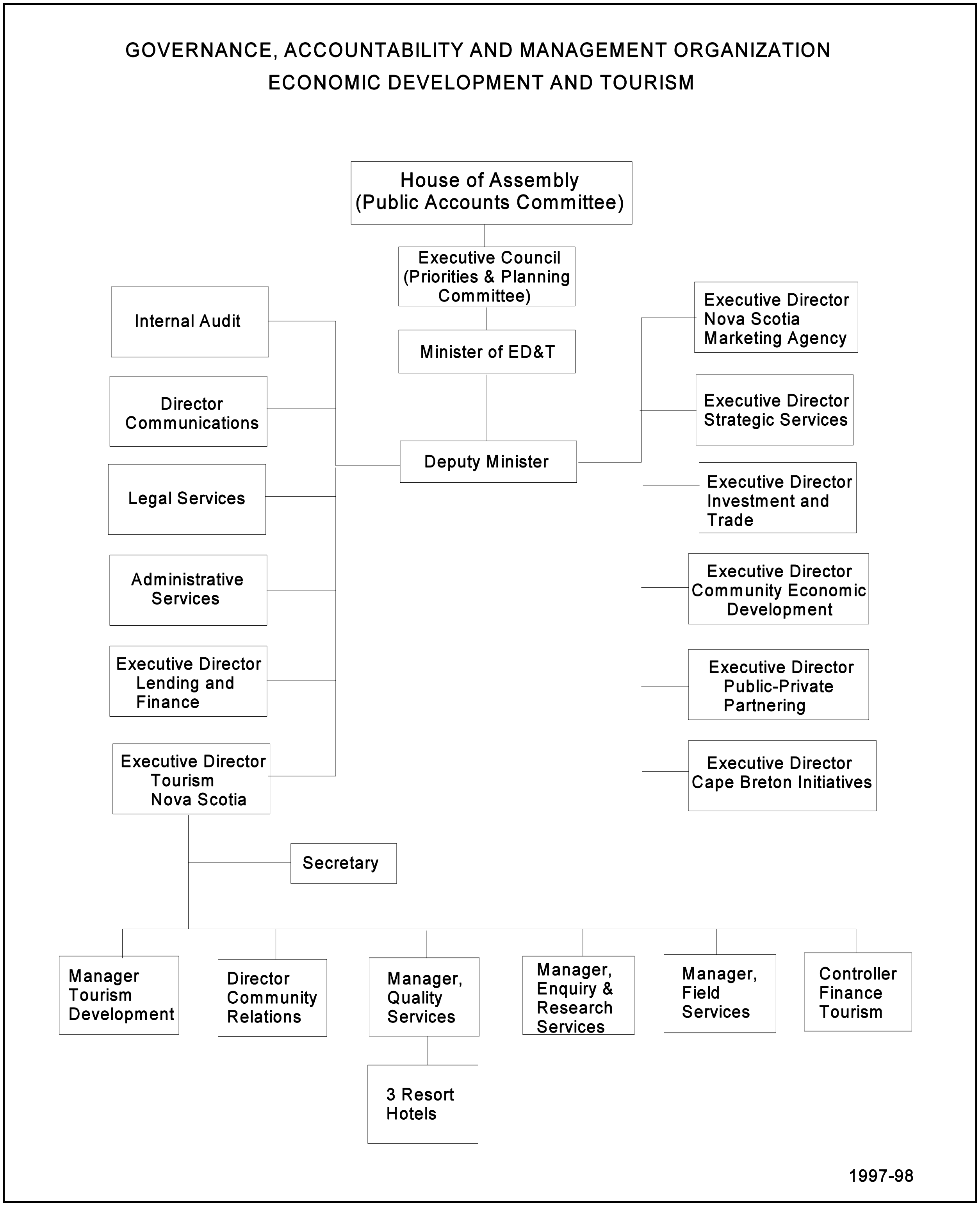

GOVERNANCE, ACCOUNTABILITY AND MANAGEMENT ORGANIZATION
ECONOMIC DEVELOPMENT AND TOURISM
House of Assembly (Public Accounts Committee)
Executive Council (Priorities & Planning Committee)
Minister of ED&T
Deputy Minister
Internal Audit
Director Communications
Legal Services
Administrative Services
Executive Director Lending and Finance
Executive Director Tourism Nova Scotia
Executive Director Nova Scotia Marketing Agency
Executive Director Strategic Services
Executive Director Investment and Trade
Executive Director Community Economic Development
Executive Director Public-Private Partnering
Executive Director Cape Breton Initiatives
Secretary
Manager Tourism Development
Director Community Relations
Manager, Quality Services
Manager, Enquiry & Research Services
Manager, Field Services
Controller Finance Tourism
3 Resort Hotels
1997-98

Exhibit 7.11

**STAKEHOLDERS IN PROVINCIAL TOURISM
WHO INTERACT WITH TOURISM NOVA SCOTIA**

Atlantic Canada Tourism Partnership

Canadian Tourism Commission

Federal government departments and agencies such as the Atlantic Canada Opportunities Agency

Regional Development Authorities

Regional Tourist Associations

Tourism Industry Association of Nova Scotia

Tourism operators such as hotels and resorts

Other divisions of ED&T, such as the Nova Scotia Marketing Agency, Community Economic Development, Investment and Trade, and Lending and Finance

Other Provincial departments such as Natural Resources and Transportation and Public Works

Exhibit 7.12

MEMBERSHIP IN THE INFORMATION AND RESERVATION SYSTEM (1997)
(Source: Staff of ED&T)

TYPE OF MEMBER	NUMBER OF MEMBERS
Fixed roof accommodations in:	
- Nova Scotia	638
- Prince Edward Island	60
- New Brunswick	54
- Newfoundland	33
	785
Campgrounds in:	
- Nova Scotia	69
- New Brunswick	1
- Newfoundland	1
	71
Car rental companies in:	
- Nova Scotia	37
- New Brunswick	4
	41

Exhibit 7.13

ANALYSIS OF EXPENSES AND REVENUES FOR
THE CORPORATEL AGREEMENT
(Source: Department of Finance general ledger and staff of ED&T)

	1994-95(11 months)	1995-96	1996-97
Expenses	$2,061,969	$2,193,010	$2,104,351
Revenues	501,396	559,299	464,440
Net Expenses	$1,560,573	$1,633,711	$1,639,911

Exhibit 7.14

PROVINCE OF NOVA SCOTIA
PROVINCIAL RESORT HOTELS
STATEMENT OF USER FEES AND EXPENSE
FOR THE YEAR ENDED MARCH 31, 1997

	Pines Resort	Keltic Lodge	Liscombe Lodge	Totals 1997	Totals 1996
User Fees					
Rooms	$1,292,226	$1,385,965	$ 583,888	$3,262,079	$3,257,820
Food	999,718	1,246,170	515,790	2,761,678	2,791,163
Beverage	202,977	212,158	65,635	480,770	470,599
Other	445,547	272,038	134,237	851,822	587,045
	2,940,468	3,116,331	1,299,550	7,356,349	7,106,627
Expense					
Salaries & Wages	1,315,317	1,453,697	658,863	3,427,877	3,282,236
Travel	18,860	14,216	3,051	36,127	23,990
Supplies & Services	1,321,556	1,288,238	542,327	3,152,121	2,926,418
Other	66,903	364,643	132,046	563,592	524,296
	2,722,636	3,120,794	1,336,287	7,179,717	6,756,940
Operating Profit	$ 217,832	$ (4,463)	$ (36,737)	$ 176,632	$ 349,687

Note: This financial statement reflects user fees and current expenditures of the Provincial Resorts budgeted under the Department of Economic Development and Tourism. $652,639 in furniture and equipment purchases, is included in current expenditures.

The following is not included in this statement: $1,092,601 in capital expenditures for construction, renovation and upgrading of facilities under Public Works and Special Projects (details of these expenditures are included in Volume 1 of the Public Accounts of the Province of Nova Scotia); $299,717 for golf course maintenance at the Pines Resort accounted for by the Department of Transportation and Public Works; $206,693 in maintenance costs accounted for by the Department of Transportation and Public Works.

(Source: Reproduced from page 235 of Volume II of the March 31, 1997 *Public Accounts*)

8.

EDUCATION AND CULTURE - PUBLIC-PRIVATE PARTNERSHIPS (P3s) FOR SCHOOL CONSTRUCTION

BACKGROUND

8.1 In the April 17, 1997 Budget Address to the House of Assembly, the Minister of Finance stated

> "*Every new school in Nova Scotia will be built through public-private partnerships. This means more schools will be built more quickly with leading-edge technology. Seven of these schools are now in various stages of planning and construction. Over the coming year, government will outline details of the next round of new school construction.*" (Budget Address to the Nova Scotia House of Assembly for the fiscal year 1997-98, page 15)

8.2 This represents a fundamental shift in the way in which schools are designed, constructed, financed, owned and operated in Nova Scotia.

8.3 The following paragraphs include background information which we believe is necessary to understand the issues associated with this transition including:

- the objectives of the public-private partnership (P3) process for school construction;
- the history of school construction financing in Nova Scotia; and
- the recommendations of the Canadian Institute of Chartered Accountants relating to accounting for leases and their impact on the financial statements of the Province.

8.4 Chapter 3 of this Report includes additional information which is also relevant to understanding the related issues such as:

- the concept of public-private partnerships (page 28);
- the Cooperative Business Solutions (CBS) procurement process (page 25); and
- the administration of the P3 process within the government of Nova Scotia (page 29).

Objectives for P3 Schools

8.5 The Department of Education's objectives for P3 schools are described in the Department of Finance Discussion Paper *Transferring Risk in Public/Private Partnerships November 1997* as follows:

> "*Schools delivered via a Public Private Partnership will be flexible, high tech learning environments to support programs and services for students during the useful life of the school. All technology will be integrated and provide valuable support tools for students and professional staff.*

These schools will be connected electronically to neighbouring schools so that equitable access to technology is accomplished.

The Private Sector will refresh the technology, and refreshed technology will be provided to other schools in the region.

One of the objectives of Public/Private Partnerships is to ensure participatory planning for the facility to accommodate programs and services both now and in the future. Students, staff, School Board, the Province, the community at large and the Private Sector are involved in the design and construction of the facility." (page 4)

8.6 In addition to Education's objectives, the Department of Finance has put forward objectives for P3 arrangements in the same publication.

"*From the perspective of the Department of Finance, the main objective for P3 is to use it as a mechanism to deliver selected services efficiently and cost-effectively so as to:*

- *attract private capital to the Province's public initiatives, thereby requiring less investment of public money;*
- *transfer expertise to the private sector, thereby creating economic opportunities in the private sector, i.e., increased private sector job creation via increased sales, both external and internal to Nova Scotia;*
- *enable the government to devote more of its resources to its "core business," the delivery of essential services;*
- *transfer risk to the private sector where this can be done in a cost-effective manner; and*
- *realize a net increase in value for public expenditures.*" (page 4)

8.7 Although not explicitly stated in *Transferring Risk in Public/Private Partnerships November 1997*, the Department of Education and Culture also has the objective of leveraging the annual appropriation available for school construction to fill as many of the urgent school construction requests from school boards as possible.

History of School Construction Financing in Nova Scotia

8.8 In the past, schools were constructed by the Department of Transportation and Public Works (formerly the Department of Supply and Services). Financing was obtained through debentures issued by the Nova Scotia Municipal Finance Corporation. When construction was complete, title to the school would be transferred to the school board and the asset and the related debt owing to the Municipal Finance Corporation would be recorded on the board's financial statements. The Department of Education and Culture would make capital debt assistance grants to the boards over the life of the debt. The grants were equal to 100% of the required payments on the debt and would be recorded as expenditures of the Province when paid.

8.9 In March 1993, to comply with pronouncements of the Canadian Institute of Chartered Accountant's (CICA) Public Sector Accounting and Auditing Board, school debt was recorded in the Public Accounts for the first time. The CICA's recommendations reflect the position that financial statements of a government should include all of its liabilities at the end of the accounting period. The Province's liabilities and net debt were increased by $217 million at March 31, 1993 to reflect this change in accounting policy.

8.10 The other effect of this change in accounting policy was that 100% of the cost of new schools would be expensed when the school was built. This new accounting treatment was consistent with that used for any other Provincial capital asset.

8.11 While the change in accounting policy was one important aspect of the history of school construction in this Province, there was a second important change at approximately the same time.

8.12 In 1992, Executive Council approved a new school construction prioritization process which included:

- requests for submissions from school boards;
- evaluation by a committee comprised of various stakeholders including school boards;
- pre-determined evaluation criteria; and
- a recommendation that $30 million be set aside annually for school capital construction to address the projects in the high priority category over the next three years.

8.13 The following shows the actual school construction expenditures of the Department of Education and Culture for the years 1992-93 to 1997-98.

Department of Education and Culture
School Construction Expenditures ($ millions)

Year	
1992-93	$54.6 - debt service grants
1993-94	$13.0 - old construction program $2.0 - new construction program
1994-95	$12.4 - old construction program $6.0 - new construction program
1995-96	$7.0 - old construction program $17.6 - new construction program
1996-97	$4.0 - old construction program $38.4 - new construction program
1997-98	$33.4 - Estimate

8.14 Fiscal restraint reduced the amount available for new school construction below the $30 million recommended by the committee. However, the demand for school construction from the public was great. It appears that the increasing public demand, combined with the Province's inability to devote required resources to this area, led directly to the exploration of public-private partnerships for school construction as a solution.

8.15 The Department of Education and Culture's estimates for the 1996-97 and 1997-98 fiscal years included $.4 million and $2.56 million, respectively, related to school lease payments.

8.16 In December 1997, Executive Council approved the school construction priorities identified in the *Report of the School Capital Construction Committee* dated September 1997. The total value of the schools and repairs called for in the Report is approximately $360 million of which $250 million relates to new school construction. The government plans to invest approximately $25 million annually in P3 leases to permit an immediate start to the school planning process.

Impact on the Province's Financial Statements

8.17 The Canadian Institute of Chartered Accountants (CICA) issues accounting standards for profit-oriented businesses and not-for-profit organizations in its Handbook. The CICA'S Public Sector Accounting and Auditing Board (PSAAB) issues Recommendations and guidance with respect to matters of accounting and auditing in the public sector. PSAAB has not yet issued recommendations on accounting for leases in public-sector organizations. In the absence of specific public-sector accounting recommendations, the CICA Handbook becomes the source of professional guidance in accounting for leases.

8.18 The CICA Handbook distinguishes two separate methods of accounting for leases depending on the terms and conditions of the specific lease. It includes guidelines for determining whether a lease should be categorized as operating or capital. The overriding principle is that the accounting for the lease should be based on its substance rather than its form. However, we acknowledge that these quantitative guidelines have tended to be applied strictly as "rules" in both the public and private sectors which might result in different accounting treatment than if the substance of a transaction had been appropriately considered.

8.19 Note that evaluation of the substance of an arrangement may include documents other than the actual lease. If other agreements covering certain aspects of the arrangement, such as the operation of the school or the renewal of technology, are an integral part of the public-private partnership then they should also be considered when deciding on appropriate accounting treatment.

8.20 A *capital lease* is a lease that, from the point of view of the lessee, transfers substantially all the benefits and risks incident to ownership of property to the lessee. An example of a capital lease would be one where ownership of the asset at the end of the lease term is virtually assured of transferring to the lessee. For example, if the lease included a bargain purchase option at the end of the lease term it would be classified as a capital lease. A capital lease would be accounted for by the lessee as an acquisition of an asset and an assumption of an obligation to reflect the substance of the transaction in the year in which the lease was signed. *In the Province's financial statements, classification as a capital lease results in 100% of the cost of a leased asset being recorded as an expenditure and a liability when the lease is signed.*

8.21 An *operating lease* is a lease in which the lessor does not transfer substantially all the benefits and risks incident to ownership of property. Lease rentals under an operating lease should be included in the determination of net income over the lease term on a straight-line basis. *In the Province's financial statements, classification as an operating lease results in payments being recorded as expenditures when incurred.*

8.22 *The impact of the accounting principles governing lease accounting is significant. If the school leases can be accounted for as operating leases, then the Province can leverage the resources available to build schools and acquire use of more new schools within the appropriation voted by* *the House of Assembly. If the school leases include terms and conditions that require accounting as a capital lease, then the Province loses the ability to leverage the appropriation to acquire the use of more schools.* Paragraph 8.16 illustrates how the Province plans to leverage an annual appropriation of $25 million through use of operating leases to provide schools with a construction cost of $250 million.

RESULTS IN BRIEF

8.23 The following are the principal observations resulting from our audit:

- As of the date of writing this Report (December 1997) the Province had not signed leases for any of the eight P3 schools although two schools were occupied. Memorandums of Agreement for two schools (O'Connell Drive and Hants East Middle) were submitted to Executive Council in December 1997 and negotiations on final leases for other schools were proceeding. Government is making changes to ensure that costs are finalized before construction starts for future schools.

- The government did not prepare a formal analysis of the advantages of P3 arrangements in comparison to the traditional approach prior to making the decision to enter into P3 arrangements for school construction. We recommend that government prepare a detailed analysis of risks and rewards prior to entering into any future public-private partnership arrangements.

- The degree of success which the Province has achieved in transferring the risks associated with P3 schools to the private sector cannot be evaluated until the lease arrangements (including operating agreements and technology refreshment) are finalized.

- The Province has stated that school leases will not be signed unless they can be classified as operating leases under CICA guidelines. This will enable the Province to leverage the resources available to build schools and acquire use of more new schools within the appropriation voted by the House of Assembly. In December 1997, the Province announced plans to use an annual appropriation of $25 million to make payments on operating leases related to $250 million of new school construction. The requirement for an operating lease precludes consideration of certain lease provisions which might have been advantageous to the Province in obtaining value-for-money. Until the leases and other agreements are finalized, we cannot evaluate the value-for-money included in the arrangements or whether the proposed accounting treatment is appropriate.

- The Province has been making advances to the P3 consortiums to finance the school construction process. The advances were made on the basis of approved progress claims with certification of the work performed. Management of the Departments of Education and Culture and Finance provided us with a legal opinion indicating that the Departments had "*sufficient statutory authority for these expenditures*" because the lease payments were included in annual appropriations. However, we believe that the Education Act is not clear with respect to the authority of the Minister in relation to P3 schools other than the right to approve plans for school buildings. Executive Council approved the Reports of the School Capital Construction Committee in which each of the P3 schools were listed as priorities but no Orders in Council were issued to approve specific construction and public-private partnership arrangements. We recommend that the legislation be clarified to indicate the type of approval required (Minister or Executive Council) for P3 agreements and construction advances.

- As one of its March 31, 1996 year-end accounting adjustments, the Department of Education and Culture created a Trust Fund of $1.7 million for Sherwood Park Education Centre in Sydney from its 1995-96 capital appropriation. The amount was charged against the Department's 1995-96 appropriation although it will be used to fund expenditures of future years.

- We cannot conclusively state that construction of P3 schools is more or less costly than traditional schools due to the many factors involved in such a comparison, and the variation in estimates impacting such an analysis. For example, the Horton construction agreement included an estimate of $28.9 million which was subsequently reduced to $27.0 million and again reduced to $25.5 million in December 1997. Department management has provided an explanation for the reduced estimate but we are unable to determine the accuracy of the estimate until construction is complete. Exhibit 8.3 provides information sufficient to enable the reader to compare certain aspects of the costs of these schools but financing, operating and other costs to be incurred over the life of these schools are not included.

- Monitoring and evaluating P3 arrangements both during and after implementation is important and we encourage government to establish an appropriate process to monitor and evaluate P3 schools which is independent of those with responsibility for the P3 initiative.

- On December 11, 1997 the Priorities and Planning Secretariat released *Partnerships & School Construction: A Review* which makes several recommendations to improve government control over P3 school construction initiatives. Implementation of the recommendations of the Review will improve controls over certain aspects of the process but will not address all of our concerns. For example, the Review does not include a comprehensive analysis of the costs and benefits of leasing versus ownership of schools. The impact of operating leases on the long-term provision of education to students in the Province and the Province's current and future financial position and operating results is significant. Operating leases will result in the ownership of the schools resting with the private sector at the end of the lease term and the costs and benefits of such leases merit thorough consideration.

AUDIT SCOPE

8.24 The objectives of this audit were to examine:

- any analysis prepared by the Department of Education and Culture to support the decision to enter into P3 arrangements for school construction;

- the selection process for private-sector partners in order to evaluate compliance with government procurement policies;

- the accounting treatment of any school leases and interim financing arrangements for compliance with generally accepted accounting principles and the Province's stated accounting policies;

- any agreements with private-sector partners to determine whether they incorporate due regard for economy and efficiency; and
- any agreements with private-sector partners to understand the nature of risk transferred from the public sector to the private sector.

8.25 The following general criteria were used in our audit.

- Prior to making the decision to enter into P3 arrangements, the Department should formally analyse the risks, costs and benefits of P3 school financing and construction versus the traditional method.
- The selection of private sector partners for school construction should comply with government procurement policies.
- Accounting should comply with generally accepted accounting principles and the Province’s stated accounting policies.
- Key terms and conditions including design, construction, financing and operating agreements should be documented in formal agreements prior to the start of construction.
- P3 arrangements should incorporate due regard for economy and efficiency.
- P3 arrangements should result in transfer of risk to the private sector.

8.26 Our audit approach was based on discussions with management of the Departments of Education and Culture and Finance and examination of documentation provided. For our audit of the procurement process, we examined detailed documentation associated with the Sydney school only.

PRINCIPAL FINDINGS

Status of P3 School Construction Initiative

8.27 There are eight P3 schools. Exhibit 8.1 summarizes the current status of those schools.

8.28 As of the date of writing this Report (December 1997) the Province had not signed leases for any of the schools. Memorandums of Agreement for two schools (Porters Lake and Hants East Middle) were submitted to Executive Council in December 1997 and negotiations on final leases for all schools were proceeding.

Analysis to Support the P3 Decision

8.29 As mentioned previously, the decision to enter into P3 arrangements for schools represents a fundamental shift in the way in which schools are designed, constructed, financed, owned and operated in Nova Scotia. We expected that the government would have undertaken a thorough analysis of the advantages of P3 arrangements in comparison to the traditional approach prior to making this significant decision, and that there would have been appropriate documentation prepared to support the analysis. In our opinion, this type of analysis is necessary to:

- ensure that the potential risks and rewards of the alternatives have been considered; and

- act as a benchmark when evaluating the effectiveness of a new policy after it has been implemented.

8.30 The government did not prepare a formal analysis prior to making the decision to enter into P3 arrangements for school construction. We recommend that government prepare a detailed analysis of risks and rewards prior to entering into any future public-private partnership arrangements.

Procurement Process

8.31 The conventional model of school construction in the Province was Design-Bid-Build whereby the Department of Supply and Services would procure the services of an architectural firm to design the school. After a design was agreed upon, the Department would request proposals for construction.

8.32 The John C. Wickwire school in South Queens, opened in September 1997, used a variation of the conventional approach which was termed Design-Build. This approach involved a single request for proposals for both design and construction services. The procurement approach used for that school was more similar to the P3 approach which included a single request for proposals for all phases of the project - design, construction, financing and operation.

8.33 The procurement process for P3 schools was based on the Co-operative Business Solutions (CBS) procurement methodology as described in Chapter 3 of this Report (page 25). As noted in Chapter 3, page 25, CBS is a procurement method whereby a supplier is selected, on the basis of qualifications and capability rather than price, to form a business alliance of shared risks, resources and benefits between the supplier and government. Cost is negotiated after the preferred supplier is selected.

8.34 The procurement process generally consisted of the following:

- There was a public call for expressions of interest for each school (Phase I).
- Expressions of interest were evaluated by a committee with broad representation, and a short list was developed.
- Those on the short list were asked for detailed proposals (Phase II).
- The detailed proposals were evaluated by a committee with broad representation.
- A private-sector partner (preferred supplier) was selected.
- Costs and leases were to be negotiated in Phase III of the selection process.

8.35 We examined the procurement process related to Sherwood Park Education Centre in Sydney to determine if it complied with the process described to us, and concluded that it was compliant in most respects.

8.36 The process for the Sydney school was competitive. The call for expressions of interest took place in July 1994. The Call for Expression of Interest stated that "*Phase I evaluations will focus on experience, technical competence, managerial ability and proven performance, as well as a vision of the proponents solution.*"

8.37 Seventeen proposals were received and evaluated by a committee with membership from the Departments of Supply and Services, Finance, and Education and Culture and the Cape Breton District School Board. The three proponents scoring highest in the evaluation were then requested to submit detailed proposals by October 1994 and those proposals were also evaluated by the committee on the basis of pre-determined criteria which had been previously circulated to the proponents.

8.38 For Phase II of the Sydney selection process, proponents were required to submit cost estimates along with their proposed design for the Centre. Cost estimates were not required for subsequent P3 schools as preparation was deemed to be a costly exercise, and costs were subject to change if the design for the school was modified at a later stage. Submission of cost information is not usually part of the CBS process.

8.39 The *Report of the Sydney Junior High School Private/Public Partnership Committee* was issued on December 19, 1994. It included the following conclusion:

> "*Each of the three proponents are technologically capable of carrying out the project and so, as can be expected, the scores are relatively close. The evaluation team noted that none of the three finalist proponents met with their expectations absolutely. The team also noted that the costs, as projected in the proposals, are in all cases higher than carrying out the project in a conventional way. However, the team believes that negotiations with the private sector partner(s) will result in value for money and a lower overall cost.*" (page 4)

8.40 The Report included the following three recommendations:

> "*The Evaluation Team recommends that:*
>
> *1.* *The province approve of the team commencing negotiations with* [the proponents who scored first and second in the evaluation] *in an attempt to reach a more favourable financial arrangement.*
>
> *2.* *The team identify the most favourable financial arrangement and make an appropriate recommendation to the province.*
>
> *3.* *If a favourable financial arrangement is negotiated by the team, work begin immediately to have the facility designed, built, financed and operated by a private sector partner.*" (page 4)

8.41 Subsequent to the issue of that Report, the third ranking proponent was advised that they were not successful and a smaller committee was formed to begin detailed negotiation with the two remaining proponents. The smaller committee included the Deputy Ministers of Finance and Education and Culture and the Superintendent of the Cape Breton District School Board. The decision of the smaller committee was conveyed to Executive Council for information in a Memorandum to Cabinet from the Minister of Education and Culture. In April 1995, TR3LC were informed that they were the successful proponent in a letter signed by the Deputy Minister of Education and Culture.

8.42 Costs and leases were to be negotiated and finalized in Phase III of the CBS process. Those involved in the process hoped that arrangements could be finalized prior to the start of construction, or shortly thereafter, but negotiations took longer than anticipated and are still ongoing. Implementation of the recommendations in the Priorities and Planning Secretariat's recently released *Partnerships & School Construction: A Review* (see paragraph 8.63) will ensure that costs are finalized before construction starts for future schools. That Review includes the following recommendations:

> "*No construction contracts for any new projects should be executed until financing is in place and leases are signed. Leases are to be public documents...The two lead departments...should...prepare Requests for Proposals that include clear financial bottom lines including the total overall cost of each project...*" (page 7)

Participatory Planning Process

8.43 One of the Department of Education and Culture's stated objectives for P3 schools is participatory planning as described in paragraph 8.5 above. We visited Sherwood Park Education Centre in Sydney and found it to be a unique, functional school which gives the school community access to current technology. During that visit, we were told that the school represents the first time that teachers and members of the community were given formal input into the school planning process. This was achieved through consultations carried out by the successful proponent.

8.44 We believe that participatory planning processes could be carried out as part of the traditional school construction process as well as under P3 arrangements. The government conducts planning based on consultation in other sectors and could have incorporated this approach in the traditional school construction process. The Department maintains that the private sector consortiums can carry out participatory planning more economically than government but the Department did not provide any analysis to support its position.

Efficiency of the Construction Process

8.45 The Department of Education and Culture believes that P3 school construction is more efficient than the traditional approach. For example, the construction period for the Sydney junior high school was nine months (from April 1996 to opening in January 1997). We believe that the amount of time required to build a school varies with the quantity and nature of resources devoted to the task, and the manner in which the project is managed. Therefore, it should be possible to increase the efficiency of the traditional school construction process to meet construction targets. The private sector has been involved with school construction in the Province for many years as project contractors and should be able to meet construction targets set out by the Department whether the arrangement is structured under traditional lines or as a P3.

Requirement for Operating Leases

8.46 The Departments of Education and Culture and Finance have been negotiating with the successful consortiums over a lengthy period but, to date, no leases have been signed. The Province and its private-sector partners have not been able to agree on lease terms which qualify for treatment as an operating lease under the CICA guidelines (see paragraph 8.21 above). If the school leases can be accounted for as operating leases, then the Province can leverage the resources available to build schools and acquire use of more new schools within the appropriation voted by the House of

Assembly. If the school leases include terms and conditions that require accounting as a capital lease (see paragraph 8.20 above), then the Province loses the ability to leverage the appropriation to acquire the use of more schools. An annual amount of $30 million for school costs can make lease payments on a number of schools if the leases are structured as operating leases, rather than cover the entire costs of just one or two new schools if the leases are structured as capital leases.

8.47 Structuring the leases as operating leases results in the current government making commitments that will govern the level of spending for the Department of Education and Culture for school construction for a number of years. The term of the leases is likely to be in the range of 20 years. As more schools are constructed through P3's, the Province's commitment of annual payments becomes larger and the flexibility, therefore, to construct new schools (and take on additional financial commitments) in the future is reduced.

8.48 Similarly, if all the operating leases expire at almost the same time, the Province may be left with a shortage of schools and forced to renew the leases at less than advantageous terms. Management of the Department of Education and Culture has indicated that operating leases provide more flexibility because of the option to not renew the lease thereby shifting occupancy risk to the private sector. The impact of operating leases on the long-term provision of education to students in the Province is an important factor when making the decision on appropriate lease terms.

8.49 We believe that introducing the requirement for these leases to be eligible for treatment as operating leases into the lease negotiations may impact the value-for-money inherent in the final lease agreement. The requirement for an operating lease precludes consideration of certain lease provisions which are inconsistent with classification as an operating lease. For example, the government would not consider a bargain purchase option to be an acceptable component of the final agreement because it would eliminate a lease from treatment as an operating lease.

8.50 Management of the Departments of Education and Culture and Finance believe that introduction of the requirement for an operating lease to the negotiation process leads to consideration of a broader range of alternatives and, ultimately, better value for taxpayers. Until the leases and other agreements are finalized, we cannot evaluate value-for-money inherent in the arrangements or whether the proposed accounting treatment is appropriate.

Risk Transfer

8.51 The government has stated that risk transfer to the private sector is an objective for P3 arrangements (see paragraph 8.6 above). The November 1997 Department of Finance Discussion Paper *Transferring Risk in Public/Private Partnerships* discusses a number of risks that could potentially be transferred to the private sector. For P3 schools, the Discussion Paper identifies the following risks:

- *Residual value risk* - the risk associated with ownership of a school building (including its residual value).
- *Occupancy risk* - the risk that the utilization rate of a facility will be more or less than expected during all, or part, of its life.
- *Operating (availability and performance) risks* - the risk associated with the operations of school buildings under P3.

- *Planning risk* - the risk that a proposed project may not meet the required standards or community needs throughout its life.
- *Design and construction risk* - the risk of cost overruns, construction delays, or design and construction flaws.
- *Regulatory and legislative risks* - the risk that a project's viability will be affected by changes in legislation.

8.52 The Discussion Paper focuses on strategies for transferring appropriate risks to the private sector partner. As indicated in the Paper "*The essence of a truly beneficial public/private partnership is the transfer of risk from one partner who has difficulty dealing with the risk to another partner who is better equipped to deal with it.*" (page 1)

8.53 The degree of success which the Province has achieved in transferring the risks associated with P3 schools to the private sector cannot be evaluated until the lease arrangements are finalized. This includes the formal lease agreements and agreements governing any other aspects of the P3 schools including school operations and technology refreshment over the lease term.

Interim Financing of Construction Costs

8.54 The inability of the Province to finalize leases could have led to delays in starting construction because the consortiums could not obtain financing for construction costs without signed leases to be used as collateral. The Province lent funds to the consortiums to avoid construction delays. Fixed construction costs were agreed upon, in advance, between the Province and the partners and funds were advanced on the basis of the fixed costs.

8.55 The advances were to be made on the basis of approved progress claims with external certification of the work performed. The process was similar to the one used in the past for schools constructed by the Department of Supply and Services. For Sydney, the firm which performed the certification of work performed was part of the consortium. This was recognized by the Department of Education and Culture as an aspect of project control that could be improved and it was corrected in subsequent schools by having the certifier employed by the Department.

8.56 The advances were accounted for as accounts receivable from the consortiums. The Department's plan was that the leases would be signed in the near future which would allow the consortiums to obtain bank financing. When financing was obtained, the consortiums would repay the debt to the Province.

8.57 As at March 31, 1997 there were no leases signed. The Province had an account receivable of $14.8 million from the consortiums related to the Sydney and Porters Lake schools. Of the $14.8 million, $11.9 million related to Sydney and $2.9 million related to Porters Lake. The Sydney receivable was 85% of the total expected construction cost of the school, and the Porters Lake receivable was 41% of the total expected construction cost of the school.

8.58 The Province decided to expense the advances on the March 31, 1997 financial statements. The stated rationale was that the Province was uncertain of being able to negotiate acceptable lease agreements for these schools in the future and, accordingly, decided to recognize the uncertainty with respect to the accounts receivable. The expenditure was recorded as a capital expenditure of the Department of Education and Culture for the year ended March 31, 1997 and was approved by an additional appropriation in April 1997.

8.59 We asked the Departments of Finance and Education and Culture for information relating to the specific legislative authority under which the advances to the consortiums were made. The advances were approved by management of the Departments of Education and Culture and Finance. Management of the Departments of Education and Culture and Finance provided us with a legal opinion indicating that the Departments had "*sufficient statutory authority for these expenditures.*" This conclusion was based on the opinion that the advances were made under the authority of the Department of Education and Culture's annual appropriation provided in the Appropriations Act, 1996. Note that this appropriation included authority for lease payments, not advances.

8.60 The Education Act does not specifically give the Minister the authority to make advances for school construction. Section 141 states:

> "*The Minister may...*
> *(f)* *after consultation with a school board, approve plans for school buildings;...*
> *(l)* *do such other things as the Minister deems necessary to carry out effectively the Minister's duties under this Act.*"

8.61 When schools were constructed by the Department of Supply and Services (DSS), the Minister of Education obtained an Order in Council which included approval of the specific construction project and authority for the Ministers of Education and DSS to "*execute such instruments as may be necessary*". Other Departments must seek OIC's to approve advances to individuals and corporations as required by legislation. Executive Council approved the Reports of the School Capital Construction Committee in which each of the P3 schools were listed as priorities but no Orders in Council were issued to approve specific construction and public-private partnership arrangements.

8.62 The Education Act is not clear with respect to the authority of the Minister in relation to P3 schools other than the right to approve plans for school buildings. We recommend that the legislation be clarified to indicate the type of approval required (Minister or Executive Council) for P3 agreements and construction advances.

Review by Priorities and Planning Secretariat

8.63 In October 1997, the Premier requested senior officials from the Priority and Planning Secretariat and other agencies of government to review the P3 school construction process to date. The purpose of the review was to "*provide analysis of the process to date, including discussion of any shortcomings, recommendations as to whether or not the process should proceed, and recommendations as to possible safeguards that might allow for a process of school capital construction involving the private sector to go forward.*" (*Partnerships & School Construction: A Review*, page 1)

8.64 On December 11, 1997 the Priorities and Planning Secretariat released *Partnerships & School Construction: A Review* which makes several recommendations to improve government control over P3 school construction initiatives including:

- "*No construction contracts for any new projects should be executed until financing is in place and leases are signed. Leases are to be public documents.*

- *No financing or other partnering arrangements should be accepted without the prior approval of the Priorities and Planning Committee and Executive Council.*

- *Future projects for school construction should follow a clearly defined process. The two lead departments, Transportation and Public Works and Education should:*

  - *determine priority order for projects*
  - *obtain cabinet approval*
  - *prepare Requests for Proposals that include clear financial bottom lines including the total overall cost of each project,*
  - *report back to cabinet for approval on selection of private sector partners,*
  - *submit all leases to cabinet for approval prior to proceeding*
  - *ensure public tendering on the construction contract(s) for the project,*
  - *oversee completion of specific projects, and*
  - *administer all aspects of lease arrangements.*" (page 7)

8.65 Implementation of the recommendations of the Review will improve controls over certain aspects of the process but will not address all of our concerns. For example, the Review does not include a comprehensive analysis of the costs and benefits of leasing versus ownership of schools.

1996 Trust Fund

8.66 As one of its March 31, 1996 year-end adjusting accounting entries, the Department of Education and Culture created a Trust Fund in the amount of $1.7 million for the Sydney school. The Fund was set up from the Department's 1995-96 capital appropriation which included an unexpended amount for the Sydney school. The trust was established in the name of the Cape Breton District School Board with the signing officers being two members of management of the Department of Education and Culture. During the 1996-97 year, $1.3 million of the Fund was advanced to the private-sector partner for the Sydney school and is included in the amount which is planned to be recovered from the consortium when the lease is signed. The remaining $.4 million is still in the Fund. Our concern is that $1.7 million was charged against the Department's 1995-96 appropriation although it is to be used to fund expenditures of future years.

Benchmarking/cost Comparisons of P3 Projects with Similar Schools

8.67 The issue of the relative costs of P3 and traditional schools has been discussed in the House of Assembly and reported in the media. We believe that it is not possible to perform a conclusive comparison of the total costs and benefits of P3 schools until all related arrangements are finalized. These arrangements include the terms and conditions governing design, construction, ownership, financing and operation of the school buildings and related technology.

8.68 However, the Province engaged a firm of quantity surveyors (Hanscomb Consultants Inc.) to perform a comparative analysis of school construction costs for P3 schools with schools constructed using the traditional method. These comparisons are referred to as benchmarking and are based on the hard costs of building and equipping similar schools with certain adjustments to make figures comparable. The adjustments include:

- *Escalation adjustment* - to reflect the increase in the general level of construction prices from the date of tender to the date of preparation of the analysis.

- *Location adjustment* - to reflect the differences in labour and materials due to location. The purpose of this adjustment is to recognize that some locations are more costly because of higher construction labour rates and such factors as transportation costs for construction materials.

- *Site differential* - to reflect the differences in cost to make the land suitable for construction. This would reflect the difference in such costs as blasting and excavating.

8.69 The benchmarking analysis also includes interim financing costs during the construction period for each alternative. The Hanscomb analysis was tabled in the House of Assembly on December 9, 1997.

8.70 We did not verify the calculation of the adjustments made by Hanscomb. The location adjustment is subjective in that it is based on general cost differences applicable to certain locations rather than actual differences in costs incurred on specific school construction contracts. It is not susceptible to audit verification. We reviewed the site differential and escalation adjustments for reasonableness but did not audit these adjustments.

8.71 Exhibits 8.2 and 8.3 include cost data for three P3 schools (Sydney, Porters Lake, and Horton) and six traditional schools. The traditional schools were chosen because they are representative of recently constructed schools.

8.72 There are several points illustrated by Exhibit 8.3 including:

- Elementary schools generally require less space per student than schools with higher grades. This difference is due to the wider range of facilities required to deliver programs at higher levels.

- The cost estimates for P3 projects in progress are variable. For example, Horton was estimated to cost $28.9 million in the construction agreement and the estimate was subsequently reduced to $27.0 million. In December 1997, the estimated cost was reduced to $25.5 million. Management of the Department of Education and Culture provided the following explanation for the most recent reduction in the estimate:

  "*The construction contract for Horton includes 'allowances' for mechanical and electrical, technology, and furniture and equipment. We are managing these allowances so that quality is maintained but the mechanical and electrical is $1 million less, technology is $.5 million less, and furniture and equipment is $.5 million less.*"

  We cannot provide an actual cost for the school until construction is complete.

- Costs of school construction vary with the size of the school. Therefore, cost per square foot is one appropriate basis of comparison. The P3 schools generally have a lower square foot construction cost, although Auburn Drive High School (built under the traditional approach) had the lowest cost per square foot of any of the schools other than Horton (based on the December 1997 estimate for Horton).

- Space per student is another factor which influences comparative costs. The recently constructed junior high and high schools include more space per student than older schools. For example, Horton High School includes about 20% more space per student (based on planned capacity) than Auburn Drive High School.

  Space per student may be calculated on the basis of planned capacity or actual enrollments. St. Andrew's Junior High is an example of a situation where the basis chosen for calculating enrollments is significant. That school was planned to have a capacity of 600 students from grades 6-9. The school board later decided to use it only for grades 7-9 with an actual enrollment of 539 for 1997-98. Exhibit 8.3 shows both planned and actual enrollments for each school.

8.73 We cannot conclusively state that P3 schools are more or less costly than traditional schools due to the number of variables impacting the analysis. Any attempt to state that one school is more or less costly than another implies that there is a common basis for comparison when a single common basis does not exist. Exhibits 8.2 and 8.3 provide information sufficient to enable the reader to compare certain aspects of the costs of these schools but financing, operating and other costs to be incurred over the life of these schools are not included.

CONCLUDING REMARKS

8.74 Staff in the Departments of Education and Culture, Finance, and Economic Development and Tourism are very enthusiastic about the benefits of P3 arrangements for school construction. They believe that the process has been a catalyst for the creation of excellent learning environments. We visited the Sydney junior high school and found it to be unique and functional.

8.75 In order to make significant decisions like the one to enter into P3 arrangements, government needs a clear understanding of costs and benefits including comprehensive risk analysis. Such an analysis is necessary to achieve good accountability and make the decision process transparent. This was not done for P3 schools, but should be done prior to making the decision to proceed with P3 arrangements in any other government sectors. The Department of Finance's November 1997 Discussion Paper *Transferring Risk in Public-Private Partnerships* is a good first step in analysing such risks.

8.76 Monitoring and evaluating these arrangements both during and after implementation is also important and we encourage the government to establish an appropriate process to monitor and evaluate P3 schools which is independent of those with responsibility for the P3 initiative.

8.77 The Priorities and Planning Secretariat recently released *Partnerships & School Construction: A Review* which makes several recommendations to improve government control over P3 school construction initiatives. Implementation of the recommendations of the Review will improve controls over certain aspects of the process but will not address all of our concerns. For example, the Review does not include a comprehensive analysis of the costs and benefits of leasing versus ownership of schools. The impact of operating leases on the long-term provision of education to students in the Province and the Province's current and future financial position and operating results is significant. Operating leases will result in the ownership of the schools resting with the private sector at the end of the lease term and the costs and benefits of such leases merit thorough consideration.

8.78 Total costs to the Province of school buildings, in the form of final leases for P3 projects, should be known prior to starting construction. Implementation of the recommendations of the Priorities and Planning Secretariat's Review should ensure that this will occur for future projects.

8.79 The eventual outcome of the P3 school construction process in terms of achievement of due regard for economy and efficiency cannot yet be determined due to the absence of signed leases. Memorandums of Agreement for two schools (Porters Lake and Hants East Middle) were approved by Executive Council in December 1997 and negotiations on final leases are proceeding. Until the final lease agreements and agreements covering other aspects of the schools including operations and technology refreshment are available, we cannot reach any firm conclusions on the value-for-money implicit in P3 arrangements for school construction or whether the proposed accounting treatment is appropriate.

8.80 We will be examining the leases and other agreements when signed and reporting the results of those audits in future Annual Reports.

Exhibit 8.1

STATUS OF P3 SCHOOLS

School	Private Sector Partner	Date of Selection of Private Sector Partner	Formal Agreements in Place	Occupancy Date (planned or actual)	Approved Construction Cost
Sherwood Park Education Centre (Sydney junior high)	TR3LC	April 1995	Pre-development Agreement - Note 5	Jan. 1997	$14.4 million
O'Connell Drive Elementary (Porters Lake Elementary)	Nova Learning Futures Inc.	Nov. 1995	MOA - Note 1 Construction Agreement Assignment	Sept. 1997	$7.4 million
Horton High School	Hardman Lindsay School Ventures Inc.	Jan. 1997	Construction Agreement Assignment	Sept. 1998	$25.5 million (Dec./97 Estimate) $27.0 million (pre-Dec./97 Estimate) $28.9 million (per Construction Agreement)
Meadowfields Elementary (Yarmouth)	TR3LC Nova	Aug. 1997	Pre-development Agreement - Note 3	Sept. 1998	$8.0 million - Note 4
Hants East Middle	TR3LC Nova	Feb. 1997	MOA - Note 1 Construction Agreement - Note 2	Sept. 1998	$17.3 million (per draft Construction Agreement)
Hants East Elementary	TR3LC Nova	Aug. 1997	Pre-development Agreement - Note 3	Sept. 1998	$7.0 million - Note 4
Amherst Regional High	______	______	______	Sept. 1999	______
Aspotogan Elementary	______	______	______	Sept. 1999	______

Note 1 - Memorandums of Agreement between the Province and the consortiums set out general parameters for leases but do not include specifics regarding financing, operating and technology renewal.
Note 2 - This Agreement was unsigned as of the date of writing this Report (December 1997). Construction on the school began in October 1997.
Note 3 - These Agreements are signed by the proponent but not by the Department.
Note 4 - These are preliminary cost estimates prepared by the Department.
Note 5 - Certain of the terms and conditions of this Agreement were not implemented.

COMPARATIVE SCHOOL CAPITAL CONSTRUCTION COSTS PER HANSCOMB REPORTS (EXCLUDING LAND COST)

	Construction								
		Adjustments (not audited by Office of Auditor General)							
School	Hard Costs	Escalation	Location	Site	Total	Technology	Government Costs	Soft Costs	Total Benchmark Costs
P3									
Horton High									
- estimate Dec 2/97	$18,500,000	$ -	$ -	$ -	$18,500,000	$ 2,000,000	$ 260,000	$ 4,756,100	$ 25,516,100
- pre-Dec. 2/97	19,500,000	-	-	-	19,500,000	2,000,000	260,000	5,256,100	27,016,100
Porters Lake Elementary	5,292,934	-	-	-	5,292,934	724,620	135,000	1,219,446	7,372,000
Sydney Junior High	10,121,495	-	-	-	10,121,495	1,525,000	250,000	2,543,847	14,440,342
Conventional									
Auburn Drive High	11,012,576	1,219,946	2,446,504	250,000	14,929,026	1,010,000	540,000	2,857,399	19,336,425
Basinview Elementary	6,373,091	714,117	-	333,580	7,420,788	945,300	420,770	1,163,432	9,950,290
Bible Hill Middle	8,000,296	-	1,200,000	111,000	9,311,296	810,600	440,000	1,703,484	12,265,380
Hebbville Junior High	7,932,776	-	1,190,000	843,000	9,965,776	1,000,000	455,000	1,942,069	13,362,845
St. Andrew Junior High	10,333,000	252,163	1,048,315	575,000	12,208,478	1,029,813	465,000	1,934,600	15,637,891
Design-Build									
South Queens Elementary	5,370,368	131,767	-	272,550	5,774,685	784,000	497,000	1,051,800	8,107,485

Exhibit 8.2

Exhibit 8.3

COMPARATIVE ANALYSIS OF SCHOOL CAPITAL CONSTRUCTION COSTS (EXCLUDING LAND COST)

School	Square Footage	Enrollments		Total Benchmark Costs (from Exhibit 8.2)	Benchmark Cost per Square Foot	Benchmark Cost Per Student	
		Capacity	Actual			Capacity	Actual
P3							
Horton High							
- estimate Dec 2/97	171,000	1,050	-[1]	$ 25,516,000	$ 149.22	$ 24,301	$ -[1]
- pre-Dec. 2/97	171,000	1,050	-	27,016,000	157.99	25,730	-
Porters Lake Elementary	48,098	450	434	7,372,000	153.27	16,382	16,986
Sydney Junior High	88,013	650	704	14,440,342	164.07	22,216	20,512
Conventional							
Auburn Drive High	128,076	950	1,129	19,336,425	150.98	20,354	17,127
Basinview Elementary	63,200	600	635	9,950,290	157.44	16,584	15,670
Bible Hill Middle	71,747	600	564	12,265,380	170.95	20,442	21,747
Hebbville Junior High	81,000	450	472	13,362,845	164.97	29,695	28,311
St. Andrew Junior High	91,619	600	539	15,637,891	170.68	26,063	29,013
Design-Build							
South Queens Elementary	52,596	530	544	8,107,485	154.15	15,297	14,903

[1] School is scheduled for completion in September 1998.

9.

EDUCATION AND CULTURE - SCHOOL BOARDS - ACCOUNTABILITY AND AMALGAMATION

BACKGROUND

9.1 There have been significant changes to the education system in Nova Scotia in the past two years, including revisions to the Education Act which became effective in 1995 and amalgamation of 22 district school boards into six regional school boards and the Conseil Scolaire Acadien Provincial during 1996-97.

9.2 The revised Act combined the former Education Act and School Boards Act, and was seen as the first major overhaul of the education legislation in 40 years. The Act was preceded by a discussion paper outlining the need for reform titled *Education Horizons - Restructuring the Education System* which was published by the Department of Education and Culture in June 1995.

9.3 The Act recognizes the role and participation of students, parents, teachers, school board members and others in the education system. Public involvement in the education process is formalized through the introduction of school advisory councils. The Act also establishes the Conseil Scolaire Acadien Provincial for the purpose of providing a French first-language program.

9.4 The Province provided $543.1 million in operating grants to the seven regional school boards during 1996-97. This represented approximately 81% of total revenue received by the boards and 77% of total Department expenditures during 1996-97. Summaries of board revenues and expenditures are included in Exhibits 9.1 and 9.2. Expenditures per student are shown in Exhibit 9.3 and student enrolment is shown in Exhibit 9.4.

9.5 During 1997 this Office examined the accountability framework for transfer payments to school boards under the Education Act, and certain aspects of school board amalgamation. The audit was conducted under Sections 8 and 15 of the Auditor General Act.

RESULTS IN BRIEF

9.6 The following are the principal observations resulting from our audit.

- The accountability framework for transfer payments to school boards is clearly defined in the Education Act and regulations. Key stakeholders in the education process are identified, together with their accountability and reporting requirements.

- Annual reports and audited financial statements are the primary accountability documents produced by the school boards. The Department has procedures in place to ensure these documents comply with guidelines established for their preparation, and that school boards are consistent in their treatment of various financial statement and budget items.

- Bridge financing was provided to two boards in 1996-97 to fund certain expenditures resulting from amalgamation, and in 1997-98 to cover deficits incurred during 1996-97. These amounts are non-interest bearing and are repayable over three to five years from future budget allocations. We have recommended that the Act be clarified with respect to the ability of school boards to incur deficits, and also with respect to borrowing funds to finance these deficits.

- The Department has no specific plans to follow up and report on amalgamation efficiencies realized and redirection of savings.

- We obtained recent information from school boards indicating efficiencies associated with amalgamation are expected to be less than the $11 million quoted in the *Education Horizons - Restructuring the Education System* document published in 1995.

- There were three severance payments to certain former district school board staff that were unusual in comparison to the other payments and do not represent due regard for economy and efficiency in the use of public funds. We recommend that, in any future amalgamations, the Province develop guidelines for payment of severance and that severance payments in excess of these guidelines be specifically approved by the relevant department. We also recommend that school boards should have written employment or personal service contracts with management employees if the terms and conditions of employment are different from those specified in relevant collective agreements and policy manuals.

AUDIT SCOPE

9.7 The objectives of this assignment were to:

- assess the accountability framework for transfer payments to school boards under the Education Act and determine whether there is compliance with key provisions of the Act;

- assess the Department's process for developing performance measures and reporting outcomes;

- determine the process for monitoring the costs and savings associated with school board amalgamation; and

- examine the most recent projections associated with implementing the recommendations of the amalgamation coordinators.

9.8 The following general criteria were used in our audit.

- The accountability framework for payments to school boards should be clearly defined in the Act and regulations.

- Payments made to school boards should comply with legislation, and controls should be in place to ensure payments made are complete and accurate.

- The Department should have a plan to review outcome measures to ensure they are complete and of continuing relevance to the Department's activities, and to report these outcome measures on a regular basis.

- The Department should have a process for monitoring and reporting the savings and costs associated with amalgamation.

9.9 Our approach consisted of interviews with staff of the Department of Education and Culture and examination of documentation surrounding payments to school boards and performance measurement. We examined the April 1997 *School Board Amalgamation - Co-ordinators' Reports* which summarize estimated efficiencies associated with school board amalgamation. In addition, we sent a questionnaire requesting information on amalgamation efficiencies and costs to management of each of the English regional school boards.

PRINCIPAL FINDINGS

Accountability - Transfer Payments to School Boards

9.10 The external accountability framework over payments to school boards is established by legislation. The Education Act and regulations define the accountability requirements for the key stakeholders in the education process and, where necessary, the reports to be prepared by these stakeholders are described in detail. Significant components of the external accountability framework are:

- The school board is to submit an annual report to the Minister. The format and content of that report is not specified in the Act or its regulations, but the format has been established and agreed upon between the regional school boards and the Department. We noted that there were transitional guidelines for the annual report for 1996-97, the first year of amalgamation. The annual reports prepared by the school boards were all received by October 15, 1997. The Department has established a committee to review these reports in order to assess compliance with the guidelines and to review the content of the boards' submissions. A program sub-committee and a finance and operations sub-committee will each review the annual reports for compliance in their respective areas, and will prepare a joint report to the Minister on their findings.

- Audited financial statements are due by July 31 each year in accordance with the Act, however, the boards required additional time to prepare these statements due to the impact of amalgamation. Five of the seven boards submitted audited financial statements by November 14, 1997. The other two boards are expected to submit their audited financial statements in early 1998.

- School boards must provide an approved budget to the Minister within 60 days of being notified of funding for the ensuing fiscal year. Boards were notified of funding on June 30, 1997 for the 1997-98 fiscal year. The budgets were all received by November 14, 1997. The delay in receipt was again due to amalgamation. Staff at the Department monitored the time frame for completion of the budgets with school board officials.

- The duties of the Regional Education Officers (REOs) are described in the Education Act. The REOs act as liaisons between the boards and the Department, and ensure the accountabilities and responsibilities described in the Education Act are discharged by relevant members of the school board community. The REOs do not verify that Provincial school curriculum is being followed - that verification process is undertaken by the Program Branch at the Department.

9.11 Payments to school boards are monitored by the Grants and Audit Division of the Department. In addition to providing funds to the boards based on their approved budgets, the Division has also established accounting policies for the school boards and included these in a

Financial Handbook. Budgets and audited financial statements of the boards are reviewed by the Division to ensure consistency in presentation, and accuracy.

9.12 Grants and Audit Division staff are also responsible for ensuring funds provided to school boards have been spent with due regard for economy and efficiency. Management acknowledged that the Division has not focussed on economy and efficiency audits due to the issues involved with amalgamation, but has plans to take a more proactive approach in planning and conducting these audits in the future. The Division is also responsible for auditing recipients of other grants provided by the Department.

Payments to School Boards

9.13 The grants provided to school boards each year are derived from a funding formula and based on recommendations to the Minister by the Education Funding Review Work Group. This Group and its terms of reference were established in 1993 although the terms of reference are modified annually by the Group members.

9.14 The Group recommends total funds to be provided to the boards for the next fiscal year, and also recommends the allocation of this amount among the funding formula components. These recommendations are noted in a formal report to the Minister, and the recommendations of the Group may be adjusted to reflect critical budget issues of the Department. School boards are provided with preliminary funding information and receive approved budgets once Executive Council approval has been obtained.

9.15 Many of the components of the funding formula are based on enrolment. The Statistics and Data Entry Section of the Department has developed audit procedures for enrolment verification. These procedures are performed annually by staff of the Grants and Audit Division and the Regional Education Officers. We verified enrolment statistics relating to 1996-97 payments to school boards for the five largest schools in the Province and found no errors.

9.16 Payments are made to the school boards monthly in advance. We tested payments made to school boards in 1996-97 and noted that the funds provided to two boards varied from the approved amounts. In addition to the approved amounts, one board received $272,500 in grants and $1,068,000 in advances to cover programming costs and the deficit of one of its predecessor district school boards; the other board received $701,200 to finance renovations to the school board's offices.

9.17 We discussed these advances with management of the Grants and Audit Division. The advances do not bear interest and are repayable over three to five years from future annual grant allocations to each of these regional boards. These repayments were to begin in 1997-98, however, both boards have been given approval to defer payments on these advances until 1998-99. We have also been informed that the Department has agreed to provide bridge financing in 1997-98 to those boards which request it to cover deficits incurred in 1996-97. Repayments on this bridge financing will also begin in 1998-99. The advances made in 1996-97 totalling $1,769,200 were recorded as accounts receivable which will be reduced when the amounts are recovered in future years.

9.18 With respect to school board deficits, the Act provides in Section 64(4) that "..*in any fiscal year a school board shall not incur or make expenditures that will result in the total of the amounts of expenditures being in excess of the total of the amounts of the school board's revenue from all sources in that fiscal year.*" Management has indicated they interpret this section of the Act to mean a school board may not budget for a deficit in its annual budget. We believe that this section also prevents a school board from incurring a deficit during the fiscal year.

9.19 In addition, we examined the Act to determine whether school boards have the power to borrow money to finance operations and were unable to locate any provisions for borrowing of this nature. We recommend that the Act be clarified with respect to the ability of school boards to incur deficits, and also with respect to borrowing to cover deficits.

Performance Measurement

9.20 *Education Indicators for Atlantic Canada* was published by the Atlantic Provinces Education Foundation and released in September 1996. We believe that it is a significant publication on outcome measures. This document will be issued every two years and will include the indicators presently being reported, and others identified as relevant to performance measurement in Atlantic Canada. The Department also publishes an annual statistical summary which contains some performance measures.

9.21 Management of the Planning and Research Division at the Department indicated that much of the information in the *Education Indicators* report was already known by the Department. For example, indicators related to academic performance were derived from the results of the standard achievement tests. However, certain non-academic indicators highlighted areas where action was required by the Department. For example, one indicator noted that 30% of Grade 8 students felt unsafe at school. As a result, a program was announced in February 1997 to provide funds for the development of school-wide programs to reduce violence and promote positive school climates. The projects receiving funds under this initiative were announced in June 1997.

9.22 Management and staff of the Department have also been involved in developing outcome measures included in *Government By Design*, both on a government-wide and Departmental level, and in the process of reporting on performance against these measures. This reporting will be included in a document titled *Nova Scotia Counts* which was to have been published in early fall 1997. Publication of this document has been delayed due to reasons more fully explained in Chapter 2 (page 14).

School Board Amalgamation

9.23 *Background* - There were many reasons for the decision to amalgamate 22 district school boards into six regional school boards and the Conseil Scolaire Acadien Provincial.

9.24 Declining enrollment, which affects school board funding, combined with fiscal restraint created significant challenges for all school boards. Especially hard hit were small rural boards, several of which were approaching the point where ability to deliver core programs and services was threatened. Amalgamation was seen as a means of achieving a more cost-effective and efficient board system and to address the problem of small boards that were no longer financially viable.

9.25 School boards, especially small boards, were finding it difficult to provide special services to students and staff such as speech pathology, psychological services and staff development. Amalgamation was seen as a means of achieving greater economies of scale to enable the delivery of these services.

9.26 The Canadian Charter of Rights and Freedoms, introduced in 1982, guarantees minority linguistic rights. Amalgamation was seen as a means of providing for these rights by providing equal French and English educational opportunities to Nova Scotians.

9.27 Page 4 of the June 1995 *Education Horizons* document states:

"*... savings from streamlined administration alone are expected to reach approximately $6 million. As well, significant additional savings of about $5 million are anticipated from more effective regional management of large budget items such as student transportation, maintenance and use of facilities, for a total of approximately $11 million in savings. Every dollar saved will be redirected to the classroom, to improve the quality of education offered young Nova Scotians*."

9.28 Staff of the Department of Education and Culture developed the efficiency estimates quoted in the *Horizons* document.

9.29 The Department hired amalgamation coordinators through a tendering process at a cost of approximately $300,000. The coordinators were responsible for working with members of the former district boards to develop amalgamation plans. The coordinators were also asked to identify opportunities for efficiencies in administration, management and operations that could be redirected to support programs and services. Coordinators were not asked to identify one-time costs associated with amalgamation. Reports from six amalgamation coordinators were submitted to the Department outlining specific efficiency initiatives that the coordinators felt were possible.

9.30 The Conseil Scolaire Acadien Provincial (CSAP) was created to give entitled parents the right to educate their children in a French first-language program. Since it was a new entity and not formed by amalgamation, the coordinator was not asked to provide efficiency estimates.

9.31 Coordinators used different approaches in preparing the efficiency estimates. Therefore Department staff, in consultation with regional board staff, prepared additional analysis to provide a board-by-board comparison. The results of the individual coordinators' reports, plus the additional Department analysis, were published in a consolidated report entitled *School Board Amalgamation Co-ordinators' Reports* in April 1997. Efficiencies reported totalled $11.1 million consisting of $10.0 million in annual efficiency savings plus $1.1 million in one-time savings from the sale of facilities.

9.32 Efficiencies associated with possible school closures were not included in the analysis because decisions on school consolidations require extensive study and community consultation and were therefore beyond the scope of the coordinators' assignment.

9.33 *Completeness of efficiency analysis* - The analysis of efficiency savings, published by the Department in April 1997, did not identify expected one-time costs associated with implementing amalgamation such as severance costs, moving expenses and the cost of facility renovations.

9.34 *Post-implementation follow-up by Department* - The Department has no specific plans to follow up and report on efficiencies realized and redirection of savings. Department management indicated that it would be very difficult to accurately calculate cost savings achieved with amalgamation due to the nature of the financial reporting and availability of records from former boards. School boards were not asked to respond, in writing, to the coordinators' efficiency estimates. One board expressed concerns about the calculation of efficiency estimates, contained in the consolidated coordinators' report, in a letter to the Department. The board informed us that the concerns were never adequately addressed by the Department. In addition, the Department has no specific plans for a post-implementation review. Such a review could report on improvements to programs and services made possible by amalgamation as well as follow-up on efficiencies realized.

9.35 Although the Department has no plans to formally report on amalgamation, Department management indicated that they carefully monitored implementation. All organization charts for central office structures were submitted, reviewed and approved before implementation to ensure appropriate administrative cost savings were occurring. However, school boards were completely responsible for determining cost savings to be implemented.

9.36 *Questionnaire sent to school boards* - We asked management of the boards for estimates of efficiencies achieved to date and those expected to be achieved in the future. We also asked board management to confirm one-time costs, including severance costs, associated with amalgamation.

9.37 We mailed a questionnaire to all six English boards. We did not mail a questionnaire to the Conseil Scolaire Acadien Provincial for the reasons cited in paragraph 9.30. All boards returned the questionnaire.

9.38 The boards reported that not all efficiency initiatives identified by the coordinators will be implemented. Some boards reported lower savings estimates for the efficiency initiatives that are planned for implementation. In total, boards identified $6.7 million in estimated annual efficiencies from amalgamation plus an additional $.8 million in one-time savings from the sale of facilities. These savings are summarized in Exhibit 9.5 on page 109. We did not verify the savings and cost estimates reported to us by the boards.

9.39 Additional costs associated with amalgamation were not considered by the coordinators. The boards, in their questionnaire responses, estimated the following costs associated with amalgamation.

- One-time severance costs of $1.5 million of which $1.0 million was funded by the Department. The Department generally funded 70% of severance costs.
- Other one-time amalgamation costs of $.9 million including office renovations, computer hardware and software changes and moving expenses.
- One-time legal costs for blending collective agreements were identified by one board but not quantified.
- Another board identified potential additional salary costs associated with wage parity for non-teaching employees estimated at $4.5 million per year for that board. Management of the Department of Education and Culture believes this figure is overstated. The actual amount will be determined by the outcome of the first collective agreement negotiations for the amalgamated boards.

9.40 Costs associated with amalgamation are summarized in Exhibit 9.5 on page 109.

9.41 Our questionnaire did not ask about the non-financial aspects of amalgamation. Department management noted the reintroduction of lengthened days for Primary grades at some boards as an example of amalgamated-related improvements to services.

9.42 *Severance payments to former district school board employees* - The questionnaires returned by the boards indicate a reduction of approximately 75 administration positions as a result of amalgamation. Of the 75 positions, severance payments were made to 34 individuals totalling $1,607,896 of which the Department cost shared $968,507.

9.43 We did not examine the employment contracts of employees who received severance payments. We understand that the decision to award severance payments to an individual and the amount of the award depended on the nature of the position and the provisions of any union or other contract with the employee. We also understand that contractual requirements were a minimum obligation and additional payments, not required by contract, could be awarded if approved by the Board. In general, the amount of any severance payments varied depending on the individual's salary and the number of years employed by the board.

9.44 There were three severance payments that were unusual in comparison to the other payments and significant enough to bring to the attention of the House of Assembly.

- The Chief Executive Officer of a pre-amalgamation school board had an unwritten contract of employment with the board which extended to the year 2000. He was advised by the Amalgamation Coordinator that his employment contract would be honoured. This decision resulted in a commitment of three and a half year's salary or $280,000 over the remaining life of the contract. He had been employed by the Board for six and a half years prior to amalgamation and the term of service included in the unwritten contract was sufficient to qualify for a pension under the Teachers' Pension Act upon completion in 2000. For the remainder of the contract period, he has been employed by the amalgamated school board on a part-time basis to work on special projects at the same annual salary as he was being paid by the pre-amalgamation board. The Department of Education and Culture is cost-sharing the salary with the amalgamated board on a 70:30 basis and it was included on a list of amalgamation-related severance payments provided to this Office by the Department.

  Prior to making the decision to cost-share the salary, the Department of Education and Culture received a letter from the amalgamated board stating that the individual had "*...a personal services contract from his former Board that guarantees employment at his current salary until December 1999.*" The Department, on the basis of that letter and a similar letter from the Amalgamation Coordinator, believed that the individual's contract with the board was in writing and legally binding, and agreed to assist the board with the expenditure.

  Our audit determined that the individual and the pre-amalgamation board had not prepared a written employment or personal services contract. However, there was a service award agreement between the former board and the employee dated September 1994 which provided for a service award payment of $60,000 plus interest in the event of: termination (other than for just cause); death; school board amalgamation or consolidation prior to July 31, 2000; or retirement. This amount has been deposited to a trust account and will be payable to the employee in the year 2000 when he retires.

  The question of whether there was a legal requirement to honour the unwritten employment contract in this situation cannot be answered without a legal opinion. We are not aware of any legal advice being sought to support the required payment.

  We have three concerns with this arrangement:

  - The school board did not have a written employment or personal service contract with this management employee although the terms and conditions of employment appeared to be different from those specified in the relevant collective agreement.

  - The Department of Education and Culture is funding this salary as a severance payment although the individual remains an employee of the amalgamated board. Salaries of all other board employees are funded by the Department as part of school board formula funding rather than through severance expenditures.

- The amount of the total payment to be received by this employee subsequent to amalgamation is significantly more than chief executive officers of other school boards received, particularly in relation to the relatively short length of service with the pre-amalgamation board.

■ Two senior contracted staff of a second pre-amalgamation board received severance payments totalling $89,577 although they were rehired by the amalgamated board on the day following severance. However, the salaries for their new positions with the amalgamated board represented significant decreases from their previous positions (reductions of 16% and 43%). The severance payments were paid from general board funds which include Provincial formula funding but were not directly cost shared by the Department of Education and Culture like other severance payments. The pre-amalgamation board sought and received legal advice and senior management of the amalgamated board has assured us that such payments were legally required.

Our concern with these payments is that, although they may have been legally required by employment contracts, they do not represent due regard for economy and efficiency in the use of public funds. Many other employees of all pre-amalgamation boards were rehired by amalgamated boards without payment of severance.

9.45 The severance payments noted above illustrate the differences in employment contracts and terms of severance which are negotiated between school boards and their employees. We are concerned by these differences because of the impact on due regard for economy and efficiency in the expenditure of public funds directed towards education. We recommend that, in any future amalgamations, the Province develop guidelines for payment of severance and that severance payments in excess of those guidelines be specifically approved by the relevant department. We also recommend that school boards formally document employment or personal service contracts with management employees if the terms and conditions of employment are different from those specified in relevant collective agreements and policy manuals.

CONCLUDING REMARKS

9.46 The revised Education Act focuses clearly on accountability in the education system and the related reporting requirements. We support the Department's efforts in monitoring compliance with this legislation through follow-up and review of accountability documents from regional school boards.

9.47 The *Education Horizons* document and the reports of the amalgamation coordinators made assertions concerning efficiencies to be gained by amalgamating 22 district school boards into six regional boards and the Conseil Scolaire Acadien Provincial. The monitoring of these efficiencies and reporting of outcomes, both financial and non-financial, are important to ensure proper accountability of the Department and to evaluate the success of the initiative.

Exhibit 9.1

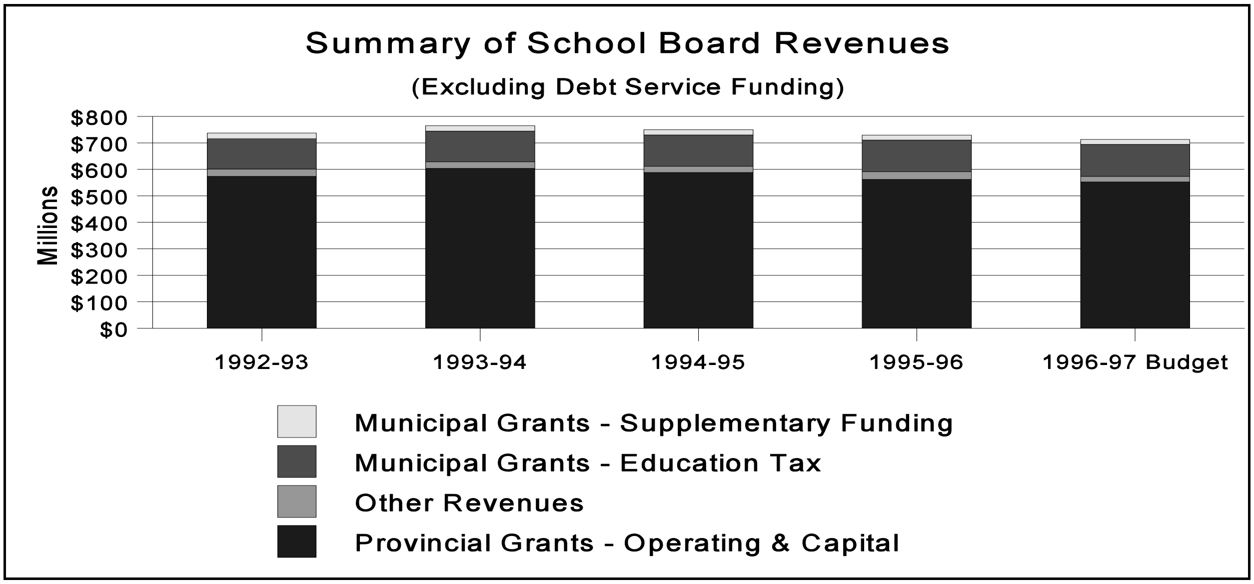


Exhibit 9.2

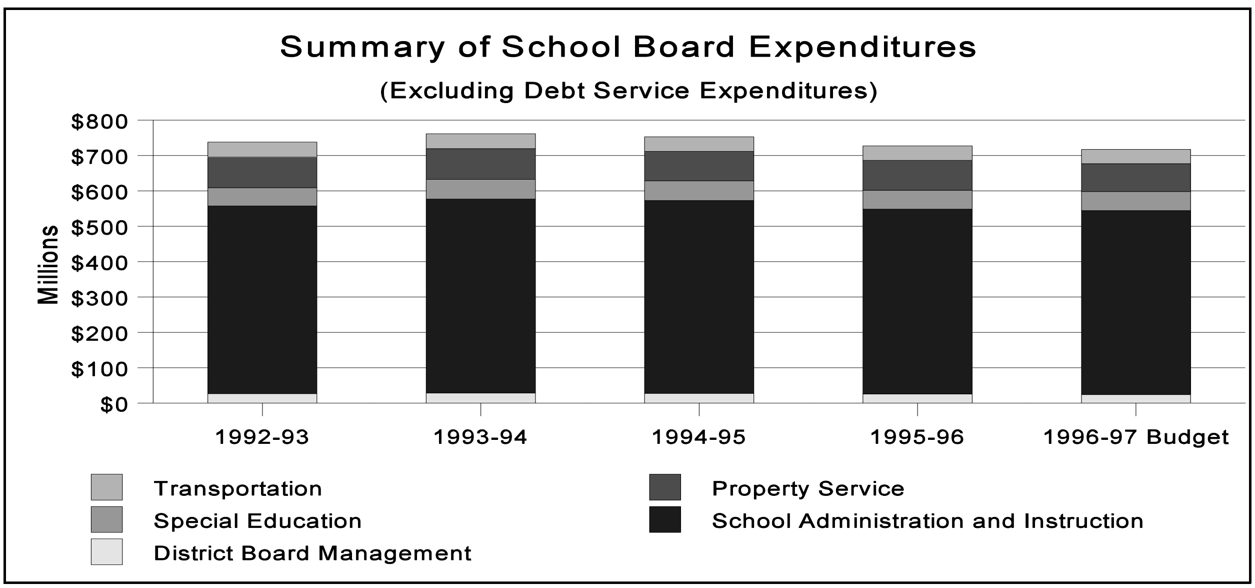


Exhibit 9.3

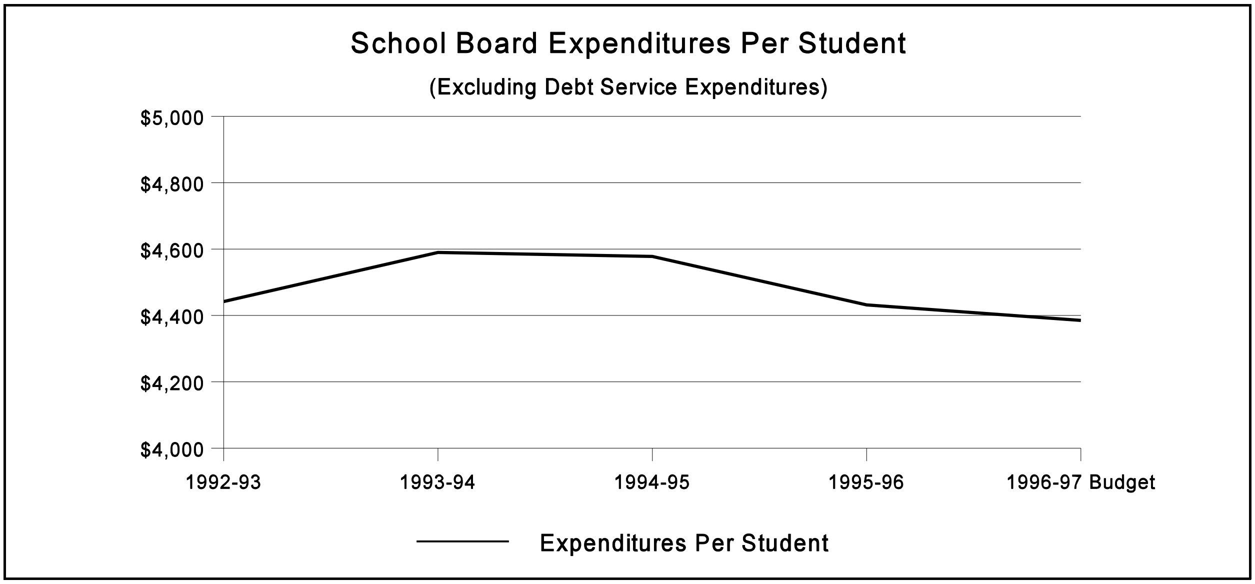


Exhibit 9.4

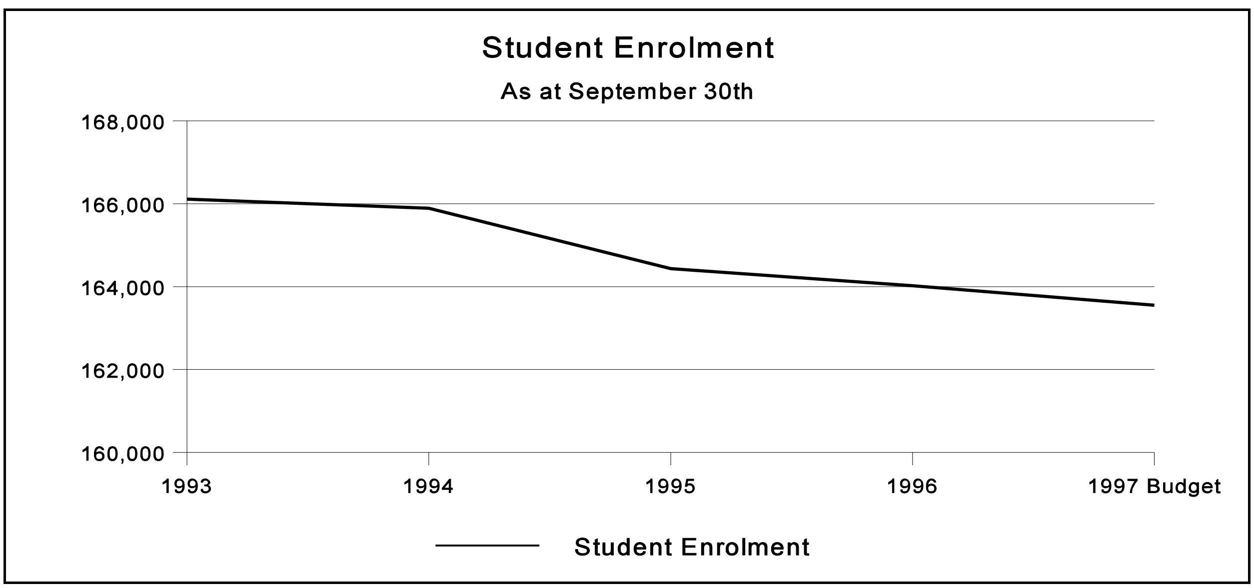


Exhibit 9.5

SUMMARY OF ESTIMATED AMALGAMATION EFFICIENCIES AND COSTS (REPORTED BY REGIONAL SCHOOL BOARDS - UNAUDITED) NOVEMBER 1997

	Annual Efficiency Estimates		One-Time Savings from Sale of Property			
Amalgamated School Board	**Per Coordinators**	**Per Board Questionnaire**	**Per Coordinators**	**Per Board Questionnaire**	**Severance Costs**	**Other Amalgamation Costs Identified by Boards**
Annapolis Valley	$ 1,388,341	$ 417,189	$ Nil	$ Nil	$ 292,536	$ 25,000
Cape Breton - Victoria	984,624	1,513,030	Nil	Nil	249,569	Note 1
Chignecto-Central	3,146,019	1,240,599 Note 2	Nil	Nil	412,000	Nil
Halifax	2,027,866	2,004,100	1,000,000	684,000	167,837	Note 3
Southwest	1,475,000	716,325	Nil	Nil	81,335	218,752 Note 4
Strait	982,656	832,700	100,000	100,000	327,947	700,000 Note 5
All Boards	$ 10,004,506	$ 6,723,943	$ 1,100,000	$ 784,000	$1,531,224 Notes 6, 7	

Note 1 - The Board reported possible legal costs for blending collective agreements. No cost estimate was provided.

Note 2 - Property services and transportation are subject to future review. Possible additional savings of $300,000 for property services and $350,000 for transportation.

Note 3 - The Board identified $4.5 million in potential annual costs to bring non-teacher salary scales to parity across the Board. Management of the Department of Education and Culture believes this figure is overstated. The actual amount will be determined by the outcomes of collective agreement negotiations.

Note 4 - The Board identified various one-time amalgamation related costs including computer hardware, software and moving expenses.

Note 5 - The Board identified $700,000 in one-time costs for construction and refurbishing of central offices.

Note 6 - Severance costs associated with amalgamation were partially funded by the Department in the amount of $968,507.

Note 7 - In addition to the above severance costs, $76,672 was paid by the Conseil Scolaire Acadien Provincial to an employee of a former board.

10.

EDUCATION AND CULTURE - STUDENT ASSISTANCE

BACKGROUND

10.1 The Student Assistance Office of the Department of Education and Culture administers the Canada Student Loan Program (CSLP) on behalf of the Government of Canada and the Nova Scotia Student Loan Program (NSSLP) for the Province. Student loans are advanced and collected by chartered banks, under the provisions of contracts with the Federal and Provincial governments.

10.2 At present, only the Royal Bank of Canada (RBC) issues Nova Scotia student loans under a two-year contract which expires January 1, 1999. Nova Scotia student loans were also issued by the Canadian Imperial Bank of Commerce (CIBC) until June 1997. The CIBC did not renew their contract which expired at that time.

10.3 The NSSLP was established in August 1993 replacing the previous bursary assistance program. This was our second audit of the NSSLP. The results of our last audit of the Program were reported in our 1995 Annual Report.

10.4 For the academic year ended July 31, 1997, the Student Assistance Office approved 18,238 Canada Student Loans and 18,217 Nova Scotia Student Loans with a value of $70.3 million and $50.3 million respectively. Exhibit 10.1 on page 118 includes several key statistics for the programs.

10.5 The administration costs of the Student Assistance Office to deliver both the CSLP and the NSSLP consist primarily of salary and data processing expenditures and totalled $2.8 million for the year ended March 31, 1997. The Province receives a contribution from the Government of Canada for administering the CSLP. During the 1996-97 fiscal year, the Government of Canada contributed $567,336.

10.6 In addition to administration costs, the Province's costs for the NSSLP consist of:

- interest on Nova Scotia Student Loans while students are studying and for six months after completion of studies (the Federal government pays the interest and other lending costs of the CSLP);

- an Interest Relief Program which provides an additional 30 month interest-free period, at any time during the repayment period, should the borrower be unemployed or underemployed;

- guarantees to the bank of repayment of student loans for those who become bankrupt or deceased at any time prior to the seventh month after the completion of studies;

- costs of the Loan Remission Program whereby a portion of a student's loan will be repaid by the Province, upon successful completion of the year's studies, to the extent that the loan for the year exceeds a predefined maximum debt level; and

- a risk premium of 5% of the amount of loans awarded, payable to the bank by the Province, to compensate the bank for assuming the risk of default by the borrower.

10.7 The costs to the Province of interest payments, loan remission grants, loan guarantees, risk premiums, administration costs and the Interest Relief Program for the fiscal years 1993-94 to 1996-97 are presented in Exhibit 10.2. Exhibit 10.3 shows lending activity for the period from 1993-94 to 1996-97.

10.8 Canada and Nova Scotia Student Loans are provided to eligible students to continue their education at the post-secondary level at designated universities, community colleges and trade schools. The amount of loan available to a student depends on the student's financial need. Financial need is the difference between assessed educational costs and living expenses, and student resources and, if applicable, parental or spousal resources.

10.9 For the 1996-97 academic year, student loans were limited to $165 per week of study under the CSLP plus $150 per week under the NSSLP. A student, with no other means of support, registered for a 34-week study period (a typical university academic year) could borrow a maximum of $10,710 each year under both loan programs. A four-year study program could accumulate debt of $42,840. The Loan Remission Program, described above, reduces student debt levels. Using the above example, the full-time university student could be eligible for loan remission of $3,560 each year. Maximum debt at the end of the four-year period could be reduced from $42,840 to $28,600. Average loan awards tend to be less than the maximum available. For the 1996-97 academic year, the average approved loan per student (CSL and NSSL combined), net of loan remissions, was $6,338.

10.10 Nova Scotia Student Loans are available only to full-time students who are residents of the Province of Nova Scotia. There is no age limit and a student may attend an institution anywhere in the world, provided the institution has been designated as eligible by the Student Assistance Office.

10.11 Under the terms of the contracts with the chartered banks, interest is paid to the banks by the Province while the student attends school and for six months after the completion of studies at an interest rate equal to the bank's prime rate plus 0.25%. Students are required to commence loan repayment after this date at an interest rate of bank prime plus 2.5% or 5% depending on whether a variable or fixed interest rate is selected by the borrower. The repayment period of a student loan can be as long as eight years depending on the amount of the loan.

10.12 The collection of delinquent accounts is the responsibility of the banks for which the Province pays a one-time fixed fee, or risk premium, of 5% of the loan balance at the time repayment by the student commences.

10.13 There is a high degree of harmonization between the NSSLP and the CSLP. There are common application forms, program guides and needs assessment processes. There are aspects of the NSSLP that are different from the CSLP. For example, the Loan Remission Program is unique to the NSSL, loans to part-time students are available only under the CSLP, and there are separate contracts with lenders. There are ongoing discussions with the Federal government concerning harmonization of student debt management programs and contracts with lenders.

RESULTS IN BRIEF

10.14 The following are the principal observations resulting from our examination.

- Based on our testing of loan advances, loan awards are calculated accurately and are supported by required documentation in the student files. The average processing time for loan applications for the 1996-97 academic year was 21.6 days.

- Based on our testing of billings from the banks, controls appear adequate to ensure billings from the banks for interest, interest relief and risk premiums are accurate and complete. We have recommended strengthening of controls over interest verification and changes to student end-of-study dates.

- Loan transaction data and loan default information from the bank are not adequate. We have recommended that deficiencies be corrected.

- There is no regular reporting of outcomes and performance standards of the Student Assistance Office. Thus accountability reporting to senior management of the Department is not adequate. Key outcome measures for the Office should be reported to the House of Assembly through the Department's annual report.

- There are no formal standards for the designation of educational institutions although draft designation criteria are now being developed. There is presently no requirement for designated educational institutions to report graduation, retention and employment rates to the Student Assistance Office. We have recommended that the Department finalize development of designation and reporting requirements for educational institutions.

- There continues to be no written agreement with the Federal government concerning the recovery of administration costs. The administration costs incurred by the Province in delivering the CSLP exceeded Federal recoveries by $459,370 for 1995-96.

- The Department has not fully recorded its liability and the corresponding expense for risk premiums on loans issued to March 31, 1997. We believe that Department expenditures and liabilities were understated by $2.7 million as a result of this omission.

- Under the terms of the financing contract with the banks, the Province assumes long-term financial obligations under the Interest Relief and Loan Remission programs. Contingent liabilities under these programs are not currently disclosed in the Province's financial statements. The loan information required to calculate the Province's financial exposure to loan remission and interest relief claims is not being gathered. There is evidence that the amounts could be significant because one bank reported a 30% default rate for student loans on repayment status. We have recommended that the required loan information be gathered and, if material, contingent liabilities should be disclosed, by way of note, to the Public Accounts of the Province.

AUDIT SCOPE

10.15 The objectives of this assignment were to:

- follow up on the results of the 1995 audit of the Student Assistance Program; and

- examine and test the systems of control over loan awards, interest relief and loan remission claims, and billings from the banks for interest and risk premiums.

10.16 The following general criteria were used in our audit.

- There should be adequate systems of control to ensure loan awards are made only:

- to eligible students;
- for eligible educational costs;
- if enrolled in designated educational institutions;
- for eligible educational programs; and
- in the proper amount based on an accurate assessment of student financial need.

■ There should be adequate systems of control to ensure that billings from the banks for interest, interest relief and risk premiums are accurate and complete.

■ There should be an established process for setting and reporting program objectives, outcomes and performance measures.

■ There should be established criteria for the designation of educational institutions.

■ There should be a written agreement with the Federal government concerning the recovery of administration costs.

■ There should be established policies and procedures for the NSSL Program.

■ Bursary overawards should be properly recorded and appropriate action should be taken to recover overawards.

■ There should be an estimated liability for risk premiums on loans advanced in the accounting records of the Province.

■ There should be adequate disclosure of contingent liabilities for interest relief and loan remission costs related to loans advanced in the accounting records of the Province.

10.17 We interviewed staff of the Student Assistance Office and tested a sample of loan applications and billings from the banks. We also examined relevant reports, student loan files and other documents.

PRINCIPAL FINDINGS

Loan Advances

10.18 We tested 40 loan applications for student eligibility, accuracy of loan calculations, proper supporting documentation in the student file and timeliness of processing.

10.19 *Supporting documentation* - For the most part, required documentation was present in the student file, the documentation supported the calculation of the loan award amount and student files were neat and organized. We did note four instances where certain required documentation was missing with no explanation or reason for the missing documents. We note that there is no checklist of required documents contained in the student file with an explanation required for missing documentation. We have recommended that such a checklist be developed.

10.20 *Accuracy of loan awards* - We found that loan calculations were generally accurate and cost and student resources were properly supported. We noted one instance where student need was understated by $2,750 because an incorrect tuition fee and text book allowance were used in the calculation.

10.21 *Timeliness of application processing* - The Student Assistance Office monitors, and has developed performance standards for, the average processing time of loan applications. For the 1996-97 academic year, the average processing time for loan applications was 21.6 days. This average does not include delays caused by following up missing information from a student's application. The standard for average processing time is 14 to 21 days.

Billings from Banks

10.22 We tested one month's billings from both the CIBC and the RBC for interest charges, risk premiums, loan remissions and interest relief. There were no claims for guarantees during the test period.

10.23 *Overall findings* - No significant monetary errors were noted during our testing of billings from the banks. The Student Assistance Office relies heavily on an edit report generated by the Student Loan System to identify potential errors in billings from the banks. The control system then depends on the thoroughness of Student Assistance Office staff in investigating the items flagged in the edit report and ensuring that monetary errors identified are corrected by the banks in subsequent months' billings. In general, controls appear to be adequate to ensure the Province only pays bona fide billings.

10.24 *Interest verification* - The Student Loan System performs a reasonableness test on the interest charged for each loan as part of the edit testing on billings. Specifically, the System estimates interest for each loan for the month based on the month-end loan balance. If the interest billed by the bank for a loan exceeds twice the estimated amount, the System flags the transaction in an edit report. In our opinion, the tolerances accepted as "normal" in this edit procedure are too broad to provide an adequate reasonableness check on interest billings. No other overall reasonableness test for interest charges is performed by Student Assistance Office staff.

10.25 *Changes to end-of-study dates* - Changes to end-of-study dates are processed directly by the banks with no prior approval by the Student Assistance Office. In addition, the banks or the educational institutions do not always provide copies of the applications for changes to end-of-study dates to the Student Assistance Office. Thus the Student Assistance Office cannot verify that changes to end-of-study dates are legitimate in these cases. Accurate end-of-study dates are important because they determine the period that the Province will have to pay interest after the student leaves school. We have recommended strengthening of controls in this area.

10.26 *Transaction and default information reported by banks* - Banks are required to supply monthly an electronic tape of transactions for each loan on interest free status to the Student Assistance Office. The Student Assistance Office uses these transactions to monitor increases to loan balances, to verify transfers from one financial institution to another and to verify continuity of the total portfolio balance upon which interest is based. The transaction data supplied by the Royal Bank does not distinguish between loan advances and transfers from other financial institutions because of programming deficiencies. Thus it is impossible for Student Assistance Office staff to adequately monitor loan transactions from this bank.

10.27 The Royal Bank does not supply loan default information to the Student Assistance Office. Risk premiums paid to the bank, currently 5% of loan advances, are based on assumptions about future repayments by borrowers. Future contracts with banks may include higher or lower risk premiums depending on actual repayment experience under the NSSLP. Monitoring loan default information is critical to negotiating appropriate risk premiums in future contracts.

10.28 We have recommended that deficiencies in the reporting of transaction data for loans and loan default information be corrected as soon as possible.

Recording Expenses for Risk Premiums, Loan Remissions and Interest Relief

10.29 *Risk premiums* - Risk premiums are payable to the banks at the time a student commences repayment of a loan. However the obligation to pay risk premiums is incurred when the loan is advanced. In our opinion, the Department should record a liability and expense for risk premiums as loans are advanced. In this way the expense for risk premiums would be recognized in the year the related loan was advanced.

10.30 For the 1997 fiscal year, the Department recorded an accrued liability of $936,158 representing estimated risk premiums on loan advances made during the 1996-97 fiscal year. However the Department did not record a liability for unpaid risk premiums on loan advances made prior to 1996-97. We estimate that Department liabilities and expenses for the 1996-97 fiscal year are understated by $2.7 million as a result of this omission.

10.31 *Loan remission claims* - There is also no disclosure in the financial statements of the Province of the exposure to additional expense for loan remissions and interest relief claims. Loan remissions and interest relief expenses are recorded in the year claims are approved.

10.32 The Department's financial exposure to loan remission claims depends on whether individual loans exceed the maximum debt levels established for the program and whether the student successfully completed studies. This can be estimated from prior years' experience. During the period April to October 1997, the Student Assistance Office approved $2.0 million in loan remissions related to loan advances made during 1996-97. This contingent liability was not disclosed in the March 31, 1997 Public Accounts of the Province.

10.33 *Interest relief claims* - The Department's financial exposure to interest relief claims depends on the value of the loan portfolio on repayment status, students' employment prospects, the average interest rate for loans in the portfolio and the average number of months that loans remain on interest relief.

10.34 Since 1993-94 there has been a conversion of $58.3 million of loans to repayment status. The Student Assistance Office could not tell us the actual value of the loan portfolio on repayment status at March 31, 1997 because this information is not reported by the banks. Student Assistance Office staff project an additional $111.5 million in conversions to repayment status by the 1999-2000 fiscal year. Therefore the portfolio of loans with the ability to attract interest relief claims could be as high as $169.8 million by the year 1999-2000. Default information reported by the CIBC in September 1997 reveals a 30% default rate for loans on repayment status. Loans in default are defined as loans that are more than two monthly payments in arrears.

10.35 It is difficult to estimate the exposure of the Province to interest relief claims based on the above information. There is a lack of information from the banks on the number and value of loans on repayment status, the average interest rate and the repayment term of these loans, the number and value of loans granted interest relief and the average number of months that loans tend to remain on interest relief. We have recommended that information be gathered to enable estimates of the Province's exposure to interest relief claims. If material, this contingent liability should be disclosed in the Public Accounts of the Province.

Follow-up to 1995 Audit

10.36 *Outcome measures and performance standards* - Program objectives, target outcomes and performance standards are not developed annually by the Student Assistance Office. We have recommended that program objectives and outcome measurement criteria be developed and that the achievement of program objectives, outcomes and performance standards be documented and reported annually to senior management of the Department. Key outcome measures should be reported to the House of Assembly through the Department's annual report.

10.37 *Regulations and policies and procedures manuals*- Regulations still have not been approved under the Student Aid Act, even though the Program has been in operation since August 1993. Management informed us that regulations are in the final stages of revision but have not been finalized. We have recommended that regulations be finalized and submitted to Executive Council for approval as soon as possible.

10.38 The Department developed a draft policies and procedures manual for the NSSLP in November 1997. We have recommended that the draft policies and procedures manual for the NSSLP be finalized as soon as possible.

10.39 *Position descriptions* - We reported in our 1995 Report that position descriptions for most key positions within the Student Assistance Office were significantly out of date. This continues to be the case. A significant organizational change during 1996-97 is the primary reason why position descriptions have not been updated.

10.40 *Performance appraisals* - We reported in our 1995 Report that no written annual performance appraisals had been prepared for staff of the Student Assistance Office. Management informed us that performance appraisals have since been prepared for two staff. However, an annual performance appraisal process has not been established and performance appraisals for the remaining 18 staff have not been completed.

10.41 *Designation of educational institutions* - The designation of educational institutions for the NSSLP and CSLP is a Provincial responsibility. The designation process is carried out by the Director of Student Assistance and approved by the Minister. There are no formal written standards for designating an educational institution. At present, an educational institution applying for designation must be registered in accordance with the regulatory requirements of the jurisdiction involved. Institutions are not required to re-certify after a period of time. There are no provisions for revoking the designation of an educational institution.

10.42 There is also no requirement for designated educational institutions to report graduation rates, retention rates or employment rates upon graduation. These factors are important to ensure the wise investment of public monies in the student loan program.

10.43 Management informed us that draft designation criteria were developed in April 1997. Management plans to discuss the criteria with stakeholders and finalize designation criteria in the near future.

10.44 *Administration cost recoveries from the Federal government* - There continues to be no written agreement with the Federal government concerning the recovery of administration costs incurred by the Province in delivering the Canada Student Loan Program. We have recommended that the Department negotiate a written recovery agreement.

10.45 The Federal government determines recoveries to be paid to the provinces. The amount of payment is based on a national budget allocation divided between the provinces on the basis of eligibility certificates issued by each province.

10.46 In June 1997, the Department received $542,336 in administration recoveries for the academic year ended July 31, 1996. Administration costs of the Student Assistance Office were $2.0 million for the fiscal year ended March 31, 1996. Department staff informed us that 50% ($1.0 million for 1996) of administration costs of the Office are attributable to the delivery of the CSLP.

10.47 Federal recoveries are not sufficient to recover the administration costs incurred by the Province in administering the Canada Student Loan Program. In 1995-96 there was a shortfall of $459,370 for the year. This situation has existed for a number of years.

10.48 *Bursary overawards* - In 1991 the Student Assistance Office commenced a verification procedure requiring students to submit income tax return information which was compared to the information filed with the Canada Student Loan and bursary application. Significant bursary overawards were identified through this procedure.

10.49 In 1995 we reported significant deficiencies in the accounting, control and collection of overawards. In addition, bursary overawards had not been recorded as a receivable on the accounting records of the Province, nor had an appropriate allowance for doubtful accounts been established. The write-off of uncollectible bursary overawards had not been approved by Executive Council as required by Section 23(1) of the Provincial Finance Act.

10.50 Management informs us that collection of bursary overawards is now being administered by the Department of Business and Consumer Services. A receivable and an allowance for doubtful accounts, of $1,274,369 and $829,300 respectively, were recorded on the accounting records of the Province at March 31, 1996.

CONCLUDING REMARKS

10.51 The principal focus of our audit this year was to assess the adequacy of controls over loan awards, interest relief and loan remission claims, and billings from the banks for interest and risk premiums. We found controls to be generally adequate in the areas examined.

10.52 We remain concerned about potential cost escalation of this program and the lack of information to enable the Department to forecast future costs. We also believe there is a need to improve accounting for program costs and the disclosure of financial commitments for the program in the Public Accounts of the Province.

10.53 The Province’s exposure to the risk of cost escalation is primarily in the areas of risk premiums and interest relief claims. These areas are affected by student debt levels, employment prospects and income levels after graduation.

10.54 Risk premiums are presently fixed, by contract which expires January 1, 1999, at 5% of loans advanced. Future risks premium rates will depend on the projected cost of loan defaults at the time a new contract is negotiated. It is therefore important that accurate and complete loan default information be gathered by the Department.

10.55 Interest relief is available to students, for up to 30 months, at any time during the repayment period of the loan. To forecast future interest relief costs accurately, it is important that the Department obtain accurate data on the balance of the loan portfolio in repayment status, the number of loans that tend to be granted interest relief and the number of months that students tend to remain on interest relief.

Exhibit 10.1

SUMMARY OF KEY STATISTICS
ACADEMIC YEAR ENDED JULY 1997

	NSSLP	CSLP
Maximum Student Loan (34 week program)	$ 5,100	$ 5,610
Average Student Loan	$ 2,760	$ 3,856
Number of Loans Approved	18,217	18,238
Value of Loans Approved	$ 50,277,115	$ 70,318,788
Portfolio Balance - Interest Free Status March 31, 1997	$ 89,332,534	N/A

Exhibit 10.2

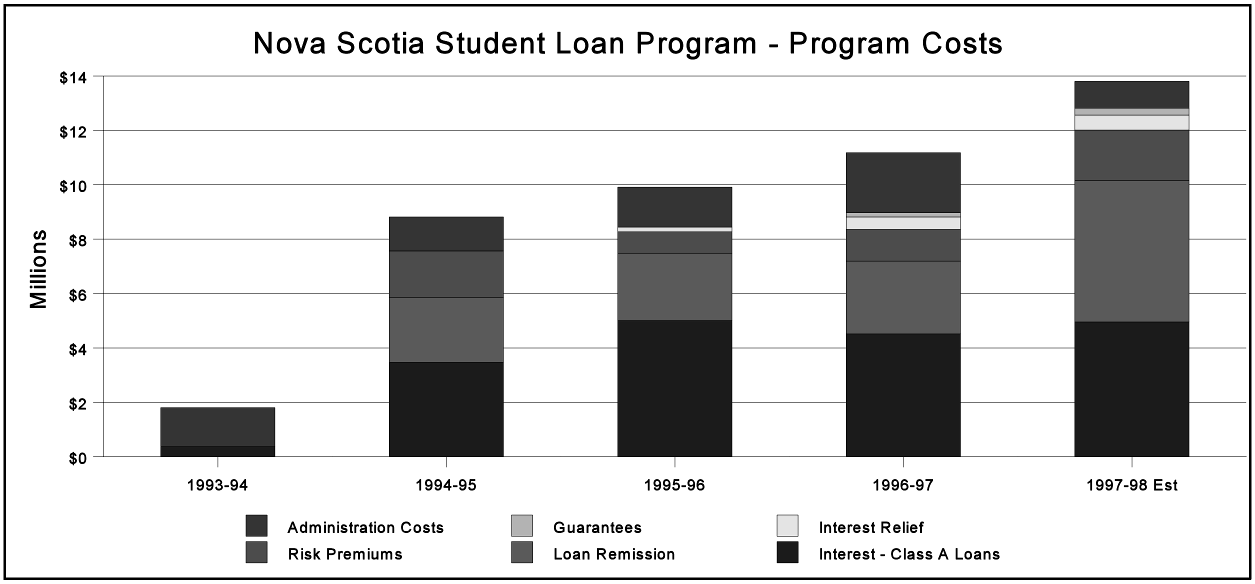
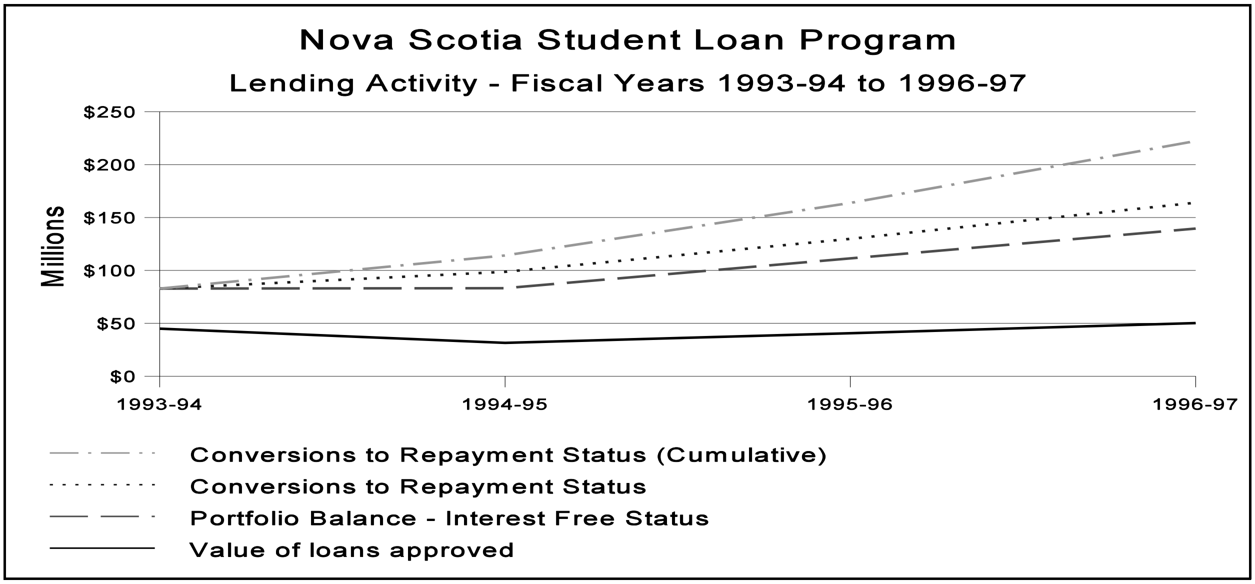


Exhibit 10.3


Nova Scotia Student Loan Program
Lending Activity - Fiscal Years 1993-94 to 1996-97
Millions
$250
$200
$150
$100
$50
$0
1993-94
1994-95
1995-96
1996-97
Conversions to Repayment Status (Cumulative)
Conversions to Repayment Status
Portfolio Balance - Interest Free Status
Value of loans approved

DEPARTMENT OF EDUCATION AND CULTURE'S RESPONSE

The Department is pleased with the findings of the recent audit of the Student Assistance Division, which determined that loan amounts had been calculated correctly and that control measures for the Nova Scotia Student Loan program were adequate. Departmental staff are currently working with the Royal Bank to improve reporting procedures and significant progress has been made to date.

The Report also identified a number of areas for improvement including outcome measures and performance standards, position descriptions, a designation of educational institutions policy and administrative cost recovery from the Federal Government. The following actions will be taken:

A) <u>*Outcome measures and performance standards*</u> *- Prior to the beginning of each processing year, the Student Assistance Division Management Team develops a Work Plan which establishes the desired results for processing turnaround time, computer enhancements, training, and staffing. The plan is adhered to and forms the basis for the operating standards in each academic year. Weekly Management Team meetings are held to monitor results and make any required adjustments. The Division will formalize appropriate measures and standards by the 3rd Quarter 1998.*

B) <u>*Regulations*</u> *- The Regulations under the Student Aid Act are in the final drafting stage by the Department of Justice and will be submitted to the Executive Council for approval during the first Quarter 1998.*

C) <u>*Policy and Procedures Manual*</u> *- This Manual will be forwarded to Senior Management for approval during the 1st Quarter 1998.*

D) <u>*Position Descriptions*</u> *- The Student Assistance Office has undergone re-engineering and organizational changes over the past four years and as a result, most of the job descriptions do not accurately reflect the tasks being performed by staff. In 1996-97, the introduction of imaging and workflow technology resulted in further changes to staff responsibilities and division organization. Preliminary work has begun to revise all the staff's job descriptions and will be completed by the third quarter 1998.*

E) <u>*Performance Appraisals*</u> *- An ongoing performance appraisal process has been established within the Department. The Student Assistance Division will be part of the Department's implementation process.*

F) <u>*Designation of Educational Institutions*</u> *- A draft designation policy has been developed. Consultations will be held among the stakeholders during the 1st Quarter 1998 prior to the new policy being implemented.*

G) <u>*Administrative Cost Recovery from the Federal Government*</u> *- A formal agreement on sharing administrative costs will be part of our harmonization process. Discussions will begin again in January 1998, with a tentative target date of August 1, 1998 for the signing of this agreement.*

H) <u>*Bursary Overawards*</u> *- The Department is pleased with the progress made to date by the Department of Business and Consumer Services in the collection of these overawards.*

11.

EDUCATION AND CULTURE - TEACHERS' GROUP INSURANCE PLANS - FOLLOW-UP

BACKGROUND

11.1 The Department of Education and Culture makes premium payments for medical, dental, life and accidental death and dismemberment (AD&D) group insurance benefits for active and retired teachers in the Province according to provisions of the 1994 Collective Agreement between the Minister of Education and Culture and the Nova Scotia Teachers Union.

11.2 Premiums paid by the Department of Education and Culture, teachers and school boards are remitted to the Nova Scotia Teachers Union (NSTU) Group Insurance Fund Trustees who are appointed by the Executive of the NSTU under the provisions of a Trust Deed dated 1965. The Province started paying premiums for the life insurance and medical plans for active teachers in 1973, for the retired teachers' medical plan in 1978 and for the dental plan in 1987.

11.3 The NSTU Group Insurance Fund Trustees (the Trustees) receive premiums and make arrangements with plan administrators and insurance carriers for insurance coverage. For the year ended April 30, 1996 the Trustees received $10.7 million from the Province and $7.2 million from plan members and school boards as premiums for the plans described above. The insurance carrier for the medical/dental plans is Maritime Medical Care Inc. (MMC) and Maritime Life is the current carrier for the life insurance plan.

11.4 The Trustees are also responsible for various other insurance plans available to teachers. For those plans, premiums are generally paid by teachers and the Province makes no contribution. Among those is a salary continuation (long-term disability) plan. The premiums for the salary continuation plan are cost-shared with teachers by some school boards under the provisions of local collective agreements between the school boards and the NSTU. Currently, the school boards fund approximately 24% of the total annual premiums of $2.5 million. The carrier for the salary continuation plan is Manufacturers Life Insurance Company.

11.5 Section 143(1) of the Education Act, passed in 1995, includes the following:

> "*The payments made by the Minister or a school board for all or a portion of the cost of any policy of insurance or any other benefits plan provided to teachers including, without limiting the generality of the foregoing, life insurance, accidental death or dismemberment insurance or medical and dental plans, are financial assistance for the purpose of the Auditor General Act and subject to audit by the Auditor General*."

11.6 In 1996 we conducted an audit of the insurance plans governed by the Trustees for which the Province or school boards cost share premiums with members. The results of the audit were reported to the Minister of Education and Culture on November 8, 1996 and included in our 1996 Annual Report (page 53). Our 1996 Annual Report noted that negotiations between representatives of the Department of Education and Culture and the NSTU with respect to insurance had commenced in November 1996 and were still in progress at the time of writing the Report. The Department of Education and Culture planned to raise other issues, particularly those related to governance of the plans, in the 1997 Collective Agreement negotiations.

11.7 This Chapter summarizes the major developments from release of our 1996 Annual Report to November 1997.

RESULTS IN BRIEF

11.8 The following are the principal findings resulting from our follow-up review.

- Negotiations between representatives of the Department of Education and Culture and the NSTU commenced in November 1996 and culminated in June 1997 with the signing of a Master Agreement and several subsidiary agreements encompassing action on many of the key findings reported in our 1996 Report. As of November 1997 most provisions of the Agreement had been implemented. The Province received $4.4 million in surplus funds from the Trustees and paid the Trustees $179,000 in September 1997 related to a deficit in the dental plan. The Agreement included referral of outstanding matters related to the Master Life Plan to arbitration with a limit of $775,000 on the amount of the dispute. An arbitrator has been appointed but a hearing has not yet been scheduled. The Department of Education and Culture has not yet nominated a Trustee as provided for in the Agreement pending the result of current Collective Agreement negotiations.

- On October 20, 1997 the Nova Scotia School Boards Association (NSSBA) requested our Office to undertake an audit of the salary continuation (long-term disability) plan to determine changes in the financial position of the plan subsequent to our 1996 audit including the current existence of surplus funds identified in our 1996 Report. The ability to achieve the objectives of the requested audit depends on full disclosure of financial information related to the plan to our Office by the Trustees and the insurance carrier. The Trustees and the carrier have agreed to cooperate fully with the audit which will be conducted in 1998 and included in our 1998 Report.

SCOPE OF REVIEW

11.9 The objective of this review was to follow-up on actions taken to address findings reported in our 1996 audit of the Teachers' Group Insurance Plans (see page 53 of the 1996 Report of the Auditor General).

11.10 Our approach included discussions with management of the Departments of Education and Culture, the NSTU, and the Nova School Boards Association and review of related documentation.

PRINCIPAL FINDINGS

Agreement

11.11 Negotiations on these insurance matters between representatives of the Department of Education and Culture and the NSTU commenced in November 1996 and culminated in June 1997 with the signing of a Master Agreement and several subsidiary agreements encompassing action on many of the key findings reported as a result of our audit.

11.12 At the time of signing of the Agreement, I issued a public statement as follows:

"*The major recommendation made by our audit was that the government undertake negotiations with the NSTU to resolve these matters. The Auditor General was kept informed as the negotiations proceeded and is pleased that the audit effort has led to resolution of this matter.*"

11.13 Key provisions of the Agreement include:

- nomination of one Trustee by the Province who will be entitled to discuss fully the financial operations of the plans with the Province;

- establishment of a new rate for premiums to be paid by the Province and school boards based on their proportionate shares of the actual costs of coverage;

- specification of the level of reserves for incurred but not reported claims;

- sharing of future deficits and surpluses in the dental and medical plans between teachers, school boards and the Province based on their proportionate shares of premiums;

- a statement that the Trustees are entitled to any future surpluses and responsible for any future deficits in the Master Life Plan;

- payment of $4.4 million from the Trustees to the Province relating to a surplus in the medical plan which had been held by the NSTU;

- payment of $179,000 from the Province to the Trustees relating to funding of a deficit in the dental plan; and

- referral of outstanding matters related to the Master Life Plan to arbitration with a limit of $775,000 on the amount of the dispute.

11.14 The financial terms of the Agreement were subject to ratification by the Supreme Court of Nova Scotia which subsequently occurred. As of November 1997 most provisions of the Agreement had been implemented. The Province received $4.4 million from the Trustees and paid the Trustees $179,000 in September 1997. An arbitrator has been appointed to deal with the $775,000 related to the Master Life Plan but a hearing has not yet been scheduled.

11.15 The Department of Education and Culture also indicated, as reported in our 1996 Report, that other issues, particularly those related to governance of these plans, would be raised by the Department of Education and Culture in the Collective Agreement negotiations taking place in 1997. Those negotiations had not concluded as at the date of writing of this Report. The Department of Education and Culture has not yet nominated a Trustee as provided for in the Agreement pending the result of the Collective Agreement negotiations.

Salary Continuation Plan

11.16 In our 1996 Report (page 57), we reported that the Province makes no payments for salary continuation plan premiums. The premiums are cost-shared with teachers by some school boards under the provisions of local collective agreements between the school boards and the NSTU. Currently, the school boards fund approximately 24% of the total annual premiums of $2.5 million. We also reported that the salary continuation plan generated approximately $5 million of dividends (net of payments to the insurance carrier) from 1978-79 to 1994-95 and that there was no agreement between the Trustees and the school boards governing the disposition of those dividends.

11.17 The salary continuation plan was not included in the June 1997 Agreement between the Province and the NSTU except in Section 5 of the Master Agreement which includes the following:

> "*(a.) The Province has no responsibility for any past, present or future deficit in or interest in or entitlement to any past, present or future surplus in the Salary Continuation Plan.*
>
> *(b.) The Province agrees that:*
>
> > *(i.) it will not act as agent of, or on behalf of, Regional School Boards or any of them, in any proceeding or action which may be brought by a Regional School Board or Boards, individually or collectively, with respect to any matter relating to the Salary Continuation Plan;*
> >
> > *(ii.) it will not provide legal counsel in connection with any such proceeding or action, and will not provide additional or special funding, pay, reimburse or assume responsibility for legal fees or other costs related to any such proceeding or action.*"

11.18 Subsequent to the release of our 1996 Report, the Nova Scotia School Boards Association (NSSBA) commenced discussions with the NSTU on the salary continuation plan. The NSSBA was authorized by the school boards making contributions to the salary continuation plan to negotiate with the NSTU on their behalf. During those discussions, questions were raised concerning the current financial position of the plans. At the time of our audit, the most recent financial statements available to us were dated April 30, 1995 and we did not review any financial information subsequent to that date.

11.19 On October 20, 1997 the NSSBA requested our Office to undertake an audit of the Salary Continuation Plan to determine changes in the financial position of the Plan subsequent to our 1996 audit and the current existence of surplus funds identified in our 1996 Report.

11.20 Representatives of the NSTU Group Insurance Fund Trustees subsequently raised concerns related to:

- the possible confidentiality of information on the financial position of the Plan;
- the potential impact of disclosure on the Collective Agreement negotiations which were currently in progress; and
- the potential impact of disclosure on the competitive position of the insurance carrier in the marketplace.

11.21 The Trustees held discussions with the insurance carrier to resolve concerns of both parties related to these issues. The ability to achieve the objectives of the requested audit depends on full disclosure of financial information relating to the Plan by the Trustees and the insurance carrier. The Trustees and the carrier have agreed to cooperate fully with the audit which will be conducted in 1998 and included in our 1998 Report.

CONCLUDING REMARKS

11.22 We are pleased to see that the Province and the NSTU, after lengthy negotiations, reached an agreement encompassing many of the findings reported in our 1996 Report. The Agreement will improve various aspects of the accountability for Provincial contributions to these plans.

11.23 We will be proceeding with an audit of the salary continuation plan as requested by the Nova Scotia School Boards Association. Results will be included in next year's Annual Report.

12.

DEPARTMENT OF FINANCE -
CORPORATE FINANCIAL MANAGEMENT SYSTEM (CFMS)

BACKGROUND

12.1 Section 7B of the Provincial Finance Act confers upon the Minister *"...responsibility for the financial management of the Consolidated Fund and related activities including ...(e) development and implementation of financial management systems for departments, where necessary..."*. Section 8 of that Act sets out a requirement that *"...The Minister of Finance shall maintain an accounting system..."*. The Act, in Section 8A, further states that *"The Deputy Minister shall determine the method of keeping all accounts of the Province and the selection of the books of account and the forms used therein."* To fulfill these responsibilities the Department of Finance maintains the central systems and accounts of the Province which record financial assets and liabilities, as well as revenues collected and expenditures incurred by government departments.

12.2 In the early 1980's the Department of Finance implemented a computerized accounting system which included a centralized recording function where departments batched transaction documents and sent them to Finance for data entry, with standard reports being produced by Finance for the departments on a monthly basis. Over the ensuing years this system evolved and matured to the point where the recording function was decentralized and departments were made responsible for the entry of transactions and provided the functionality to produce their own reports.

12.3 That system, which was primarily comprised of the general ledger, accounts payable and commitments modules, was replaced effective April 1, 1997 by a new corporate financial management system (CFMS).

12.4 In 1995, Department of Finance staff developed a departmental business analysis to provide a framework for identifying departmental and government-wide opportunities to redesign business processes and to utilize supporting technology. One opportunity identified as a priority was the acquisition and implementation of a new, fully-integrated financial management system to gather, accumulate and summarize the financial transactions of the Province.

12.5 In October 1995, the Department issued a request for proposals to *"...Supply the application and operating software/hardware and provide professional staff to implement a corporate financial management system for the Province of Nova Scotia"*. This tender was awarded in March 1996. The application software selected was *Systems Applications and Products in Data Processing (SAP)* and the proponent selected was *Deloitte & Touche Consulting Group / ICS*. As stated in an October 10, 1996 CFMS project bulletin *"...Nova Scotia is the first province or state in North America to implement SAP"*.

12.6 The vision for the project as stated in the same CFMS bulletin was *"...A fully integrated Corporate Financial Management System, will effectively transform the manner in which we conduct the financial business of government in the future, provide for enhanced decision making, provide for improved cost control, and establish the foundation for streamlining processes and procedures..."*.

12.7 The SAP application, which resides on computers at the Department of Finance, consists of a number of new and integrated modules for general ledger, budgeting, funds management, cash management, accounts payable, project accounting, procurement, goods receipt, inventory, and accounts receivable. Software licenses for the payroll and related administration systems modules were not acquired. These functions continue to be processed through the Province's existing human resource management system (HRMS), which runs at the Systemhouse Data Centre. SAP is considered compliant with regards to the global Year 2000 issue (a topic which is discussed in Chapter 4 of this Report).

12.8 Certain of the costs of CFMS were funded by the Innovation Fund which is an internal government fund created in 1995 by a special warrant. The fund is administered by the Priorities and Planning Committee and *"...provides resources required for the initial design and development of projects which will provide improved government program and service delivery together with resulting cost savings."*

RESULTS IN BRIEF

12.9 The following are the principal observations as a result of our review coverage to date.

- The CFMS project costs identified of approximately $3.9 million do not include the costs for computer hardware and the many government staff assigned to the project.
- CFMS was implemented on April 1, 1997 as scheduled. However, we have been made aware of implementation and control issues that were not fully dealt with before April 1, 1997. Certain of these had not been addressed or resolved some eight months after implementation, and may represent significant risk to the system of internal control as it relates to the accounting for public funds.
- Finance and this Office have agreed to commission an independent audit assessment of the CFMS implementation and controls. This work is to be conducted in early 1998.

SCOPE OF REVIEW

12.10 During 1997, this Office commenced a preliminary review of CFMS and the CFMS project. The objective was to gather project-related documentation and information, and to identify and develop lines of inquiry to support our planning for more detailed audit coverage.

PRINCIPAL OBSERVATIONS

Project Costs Not Complete

12.11 Based on the information provided to us by Finance, the costs of the CFMS project were approximately $3.9 million, comprised of the following:

Consulting services	$2,225,000
SAP software licenses	1,260,000
End user training	280,000
Innovation fund interest	171,000
	$3,936,000

12.12 The above does not include all internal and external costs associated with the CFMS project. For example, costs associated with computer hardware and the numerous personnel from across government who participated in the project were not included.

12.13 Costs of approximately $3,588,000 including interest were funded by borrowing from the government's Innovation Fund. This amount is to recovered from departments and repaid to the Fund over a four-year period.

12.14 In an effort to provide for repayments to the Innovation Fund, the Department of Finance, in consultation with finance directors from across government, established a formula by which the sum will be collected from government departments and agencies over a four-year period commencing in 1998-99. We have reviewed this formula and advised Finance senior management of specific concerns we have in the method of allocation and in particular how it affects this Office. They have taken the matter under advisement and are currently considering various alternatives in an effort to resolve this issue.

Project Timetable and Resourcing Restrictions

12.15 CFMS is one of the most significant IT projects undertaken by the Nova Scotia government. Commencing in April 1996, an extensive project organization was assembled, which included the secondment of many staff from across government. The target for implementation was April 1, 1997.

12.16 In regards to the overall project management organization and structure, the project planning documents identified the need for a full-time project manager. However, soon after the initiation of the CFMS project, another unrelated government initiative impacted significantly on the availability of the designated CFMS project manager.

12.17 The establishment of the corporate service units (CSUs) for the management and delivery of government's common programs and services became a major project. The CFMS project manager was appointed Director of Information Technology for the Finance CSU. This reorganization made the Finance CSU responsible for three other departments and several other government entities. The CFMS project manager, in the additional role of Director of the CSU, became directly responsible to six deputy ministers for the acquisition, deployment and support of information technology resources in those organizations. Furthermore, as the CSUs were being established, there was a significant requirement for recruiting the necessary management and staff to establish the CSU and enable it to fulfill its responsibilities.

12.18 As the result of this significant government reorganization, the CFMS project manager was unable to focus full-time on the project during the standard working day. Documentation indicates 60% of the manager's regular time was spent on CFMS and was supplemented by on-going overtime hours. Certain of the project-management related matters were delegated to the project integration managers.

12.19 Further, it is also important to note that during the project there were personnel changes at Finance in senior management positions, certain of which had key project responsibilities.

12.20 As a final matter, throughout the 1996-97 year and especially during the last six months prior to implementation, staff assigned or seconded to the project worked to complete all of the required phases and tasks. Project management and staff worked numerous nights and weekends, and for this effort they are to be commended.

Project Implementation and Control Issues Not Fully Addressed

12.21 The CFMS was implemented on April 1, 1997 as planned. However, we have been made aware of several implementation or control issues that were deferred. Many of these still had not been addressed or resolved some eight months after implementation, and some may represent significant risk to the system of internal control as it relates to the accounting for public funds. We advised Finance management of our concerns and are awaiting information as to how and when these matters will be resolved.

12.22 It should be noted that, throughout the project life cycle, a separate *Quality Assurance Program* (QAP) with the objective *"...to evaluate and report on whether the system's functional and quality requirements are being met"* was in place. This involved assessing the adequacy and completeness of the project plans for each module or phase, system design and controls, security, documentation and training. Responsibility for the QAP was assigned to the internal audit team which included a representative from the consulting firm. Documentation provided to us indicates this team was very active and produced detailed reports at the completion of each phase review. This team also identified and reported most of the implementation and control issues about which we are concerned.

12.23 We have agreed with Finance management, who share our concerns regarding the level of control, to jointly contract specialist audit resources proficient in the assessment of SAP installations and control. This project will include participation by our staff and Finance's internal audit staff in order to achieve cost-effective knowledge transfer, and is to be completed and reported around March 31, 1998.

12.24 The Request for Proposals for this audit identified the basic requirements as follows:

> *"Assessment of the adequacy of controls currently in place...and the related risks and benefits realized, along with specific recommendations for future opportunities for improvements, and this will also include assessing the decentralization/distributed controls and procedures in departments of government.*
>
> *Assessment of the current state of the post implementation and management of the new system and related controls and procedures, including consideration of management's plans, resourcing and scheduling for addressing outstanding or identified concerns."*

12.25 Management responsible for CFMS have expressed a very positive reception to this audit and view it as an opportunity to obtain an independent assessment which will also assist them in focusing their future management and support efforts. The audit will also provide this Office with information to support the planning for future audits of departments and agencies using CFMS in regards to the adequacy of controls.

Departure of Key Project Staff

12.26 Many CFMS project staff received extensive training and exposure to the system before it was implemented. These staff became proficient in the use of the system, and certain of them had assumed key management or functional roles for the future management and operation of the system.

12.27 In the early fall of 1997, only a few months after implementation and at a time when several significant implementation and operational issues were still under consideration or in the process of being addressed, several key project staff were hired by private sector entities which left the government critically short of staff skilled in the management and support of the CFMS. Many of the outstanding issues had to be deferred which delayed Finance's schedule and directly impacted on the availability of management to conduct other functions.

CFMS Training Program

12.28 CFMS project staff received extensive training and exposure to the system before it was implemented. Some of these staff, through their acquired proficiency, were assigned the task of developing and delivering detailed training sessions for other government staff. The resulting training programs focused on each of the major system modules and were initially delivered over a few months commencing in early 1997. There are additional offerings of this training as and when required by the departments.

12.29 There has been some concern expressed by departments regarding the CFMS reporting capabilities and training specific to the reporting function. If department and program management staff are not fully capable of utilizing the system's reporting functionality, the realization of benefits and savings from the new system will be impaired.

12.30 We were informed that Finance recently sent out a survey to departments to determine the current comfort levels of staff assigned to use the system. The survey results will soon be analyzed and an action plan developed to address the issues identified. As a minimum, additional training should be developed and delivered to address any deficiencies which may be identified.

12.31 In addition, we have been informed of several other initiatives focusing on improving the system reporting functions, including:

- support staff have completed additional training in the development of reports;
- third party tools are currently being reviewed which may assist users in the area of ad hoc reporting; and
- a consultant has been contracted to write various customized reports.

CONCLUDING REMARKS

12.32 In terms of costs and schedule, the acquisition and implementation of the CFMS is one of the most significant IT projects undertaken by the Nova Scotia government. This Office recognized the significance of this project and its impact on the government and in particular the financial management systems and practices. Accordingly, in 1997 we commenced a preliminary review of the system and the project itself. However, we were unable to complete this work as relevant information could not be obtained on a timely basis.

12.33 Finance management has had to focus its efforts on system management and operational support due in part to the untimely departure of several key staff who had been directly involved in the CFMS project.

12.34 Finance management and this Office have identified concerns regarding the level of control over CFMS and have decided to contract for a special audit assignment. It is intended to be completed and reported upon around March 31, 1998. Management responsible for CFMS have expressed a very positive reception to this audit and view it as an opportunity to obtain an independent assessment which will also assist them in focusing their future management and support efforts.

13.

FINANCE - DEBT MANAGEMENT - UPDATE REVIEW

BACKGROUND

13.1 According to the Province's traditional non-consolidated *Financial Statements* for the year ended March 31, 1997, net debt servicing costs (i.e., gross debt service costs, net of sinking fund earnings and public debt retirement fund earnings) were $687.2 million, 16.2% of the government's expenditures. Debt servicing costs remain the third largest category of Provincial government expenditure, after health and education.

13.2 Exhibit 13.1 on page 138 provides a summary of the debt and related funds reported on the Province's *Statement of Financial Position* as at March 31, 1997. The debts and obligations of a number of crown agencies, approximately $1 billion guaranteed by the Province (see note 7 to the Province's March 31, 1997 financial statements), are not yet specifically covered by the Department of Finance's *Debt Management Plan* which is published each year as part of *Government By Design*.

13.3 The Provincial Finance Act and the annual Appropriations Act establish the statutory requirements, authorities and limits for Provincial borrowing. Under these Acts, Executive Council has the delegated authority and responsibility for approving Provincial borrowing, including any guarantees of borrowing by crown agencies.

13.4 The Department of Finance, through its Investments, Pensions and Treasury Services Branch, is responsible for the ongoing management and control of the Province's debt and related sinking funds and the Public Debt Retirement Fund (PDRF). Finance develops and maintains cash flow plans identifying the funds required to be borrowed during a fiscal year to support government's programs and to meet its other obligations. To meet cash requirements, the Province issues a variety of debt obligations in a number of capital markets including lines of credit with major Canadian banks.

13.5 Our 1994 and 1995 Reports included chapters on the results of our review of Finance's policies and practices for managing the Province's debt and debt-related activities. During 1996 and 1997, we continued to monitor Finance's plans and progress in this significant area.

RESULTS IN BRIEF

13.6 The following are the major observations resulting from our update review procedures.

- Cost-effective management of the Province's debt and debt-related costs remains a priority for government. The size of the Province's total debt together with the significant proportion of the debt payable in foreign currencies (more than 50% as at March 31, 1997 - see Exhibit 13.1) warrants a high level of reporting to and attention by government, the House of Assembly, and the public.

- The objectives, strategies and initiatives outlined in the *Debt Management Plan* included in the government's *Government By Design* publication are significant and continue to provide a formal and improved basis to hold Finance accountable for debt management activities and results. To achieve the goals and targets set out in the *Debt Management Plan* and *Government By Design*, government must ensure that the resources available are sufficient to support implementation of necessary improvements and to ensure monitoring and reporting are timely, accurate and effective.

- Action has been taken or is planned to address many of the comments and suggestions included in our previous Reports. However, continued effort will be required to fully implement the policies, maintain plans, and implement systems necessary to support improved and continued control of the Province's debt and debt management activities on an ongoing basis.

  Draft policy statements on debt management and on the use of derivatives were prepared and substantially implemented by Finance in 1997. Finance indicated these will be finalized and presented to the Public Accounts Committee in 1998. We recommend such policy statements be subject to Executive Council approval prior to being finalized.

SCOPE OF REVIEW

13.7 The objective for this update review was to obtain current status information on the action taken or planned by Finance to improve the Province's debt management policies and practices. We also wanted to provide summary information on the Province's debt and debt management function in order to support increased awareness and understanding by the Members of the Legislative Assembly (MLAs).

13.8 Our approach included meetings with Finance management and review of available supporting documentation to determine the status of action taken or planned for the debt management related comments and suggestions included in our previous Reports.

PRINCIPAL FINDINGS

Introductory Comments

13.9 Exhibit 13.2(a) on page 139 provides a summary of the governance, accountability and management organization for the control of the Province's debt and debt-related activities.

13.10 The overall roles and responsibilities of the Executive Council, the Minister and the Deputy Minister with respect to the Province's debt and related activities are defined in the Provincial Finance Act and the annual Appropriations Act.

13.11 The Director of Liability Management and Treasury Services is responsible for monitoring the market and making recommendations to the Executive Director, the Deputy Minister and the Minister on the timing, terms, costs and sources of new borrowing. The Executive Director and his staff collaborate in the completion of negotiations with the underwriter(s) for new debenture issues, and in the completion of other significant debt-related transactions. The accounting and related activities associated with the reporting of the Province's debt in its financial statements are the responsibility of the Controller, who also reports to the Deputy Minister of Finance.

13.12 Since 1993 there has been a turnover of almost 100% of the senior staff at Finance responsible for the administration and ongoing management of the Province's debt. The Liability

Management and Treasury Services division was at full staff complement in November 1997 for the first time in a number of years.

Historical Overview

13.13 *Debenture and other commercial debt* - Exhibit 13.3 on page 140 shows the total commercial debt reported in the Province's financial statements from 1985 to 1997. As at March 31, 1997 commerical debt was $10.514 billion, up from $4.263 billion in 1985, but down from a reported high of $10.744 billion as at March 31, 1995. The Exhibit also shows the net commercial debt (i.e., total commercial debt less sinking funds and the Public Debt Retirement Fund). It is important to note that some of the change in reported debt relates to changes in foreign exchange rates from one year to the next.

13.14 The Minister of Finance's annual *Financial Report - Hitting the Targets*, which was released in August, and the *Debt Management Plan* included in the 1997-98 *Government By Design* publication provide trend information on selected measures.

13.15 *Debt servicing costs* - Exhibit 13.4 on page 141 shows the annual cost of servicing the Province's debt (i.e., debenture interest and other debt charges) for the last eight years on the same basis used for the Province's March 31, 1997 non-consolidated financial statements. The Exhibit also shows debt charges net of income from both sinking funds and the Public Debt Retirement Fund.

13.16 Debt servicing costs have increased at a higher rate than total government expenditures. During the eight-year period ended March 31, 1997, the net debt servicing costs reported in the Province's financial statements have risen 56% from $440 million to $687 million. For the same period, expenditures (current and capital) increased 6% from $3.982 billion to $4.238 billion. Net debt servicing costs absorbed 16% of total revenue for the year ended March 31, 1997 compared to 11% in 1989-90, but down from a peak of 20% in 1994-95.

13.17 Finance's *Debt Management Plan* includes information on the sensitivity of the Province's debt servicing costs to changes in interest and foreign exchange rates. The following information is extracted from the *Debt Management Plan* (per page 37 of the 1997-98 *Government By Design* publication) from a section entitled *Debt Servicing Cost Sensitivity Analysis*.

Change in Financial Market Variable	***Change in Debt - Servicing Cost (C$ Millions)***
1% Change in Canada 3-Month Treasury Bill	*18.2*
1% Change in Canada 10-Year Bond	*4.0*
1% Change in U.S. 3-Month Treasury Bill	*4.5*
1 Canadian Cent Change versus 1 US Cent	*3.4*
1 Japanese Yen Change	*1.6*

13.18 It should be noted that the impact of small shifts in interest or foreign exchange rates on the costs to the Province can be larger than the total annual costs of some departments and agencies of government.

13.19 Due to a combination of lower interest rates, fluctuations in foreign exchange rates and more active debt management, the Province’s debt servicing costs have been under budget in recent years. Within the context of government’s fiscal targets, positive budget variances for debt servicing costs in recent years have offset certain over-expenditures in other program areas.

13.20 *Foreign exchange exposure* - Foreign exchange exposure is the proportion of debt outstanding in foreign currencies to the total debt outstanding from all sources. The foreign exchange exposure differs depending on whether it is calculated on the basis of gross debt or net debt (i.e., gross debt less sinking funds and public debt retirement funds).

13.21 The Provincial Finance Act, Section 52A, includes the terms *“public debt”* and *“total public debt”*, however neither term is defined in legislation. The *Debt Management Plan* defines the term *“gross debt”* (page 41of the 1997-98 *Government By Design* publication) as:

> *“Outstanding debentures, short term promissory notes net of related investments, debt associated with hospitals and public schools, and debt assumed for Teachers’ Pension Fund, and Members’ Retiring Fund. The amount does not include the deficiency in net assets of the Crown Corporations, Nova Scotia Resources Limited and Sydney Steel, nor certain pension liabilities.”*

13.22 The Department of Finance’s *Debt Management Plan* measures foreign exchange exposure on the basis of gross debt adjusted for foreign currency swap contracts and certain pension liabilities. On this basis, as used by the Department of Finance, foreign currency exposure was 52% at March 31, 1997.

13.23 Exhibit 13.1 provides a summary of debt, sinking funds, public debt retirement funds and net debt together with the proportion in foreign currency in various categories. Using the net debt basis, the foreign exchange exposure would be 59% compared to 52% on the gross debt basis.

13.24 Exhibit 13.5 on page 141 shows the Province's foreign exchange exposure on both a gross and net basis over the last eight years. The Province’s foreign exchange exposure at March 31, 1997 was 59% - net (52% - gross), up from 50% - net (50% - gross) in 1990 and down from a 1995 peak of 71% - net (64% - gross).

Summary of Key Initiatives Taken or Planned since our 1995 Report

13.25 The 1994 chapter included a number of comments and suggestions for improvements to the debt management function and related activities. In 1995 we provided detailed follow-up comments on the action taken or planned by Finance to address the concerns and suggestions included in our 1994 Report. Based on information provided to us in 1997 by senior management at Finance responsible for Liability Management and Treasury Services, further progress has been achieved, as outlined below.

13.26 Draft policies related to debt management and derivatives have been prepared and are being used. It is anticipated that these policies will be finalized early in 1998, and Finance indicated that they will then be presented to the Public Accounts Committee. It should be acknowledged that these are working policies, and as such will continue to evolve over time. This notwithstanding, in our view the policies should be subject to review and approval by the Executive Countil.

13.27 There has been an increase in the use of alternative financial instruments (i.e., derivatives), as part of Finance’s plans which call for more active management of the Province’s debt. Finance management has informed us that all of these transactions have been conducted within the context of the draft policy on derivatives.

13.28 An internal committee structure outlined in the draft debt management policy (see Exhibit 13.2(b) on page 140) has been put in place. The individual committees are in various stages of implementation of their respective roles and responsibilities, and it was indicated to us that certain sub-committees, such as the Cash Forecasting Sub-committee, have been functioning for over two years.

13.29 In November 1997, all key management positions within the Liability Management and Treasury Services Division had been filled for the first time in a number of years. It was indicated that this will allow for more efficient management and more appropriate task delegation, including further improvements in systems and controls.

13.30 Senior management at Finance indicated that an objective of the Investment, Pensions and Treasury Services Branch is to become a centre of excellence for treasury-related matters within the Provincial government operations. This expertise would be utilized to provide proactive treasury-related support to departments, crown corporations and other public sector entities. In this regard, we note that the draft policies referred to above do not, but should, include comments on applicability to other than government core (i.e., Finance and other departments) treasury activities.

13.31 Recent amendments to the Provincial Finance Act include the following and should serve to support debt management activities and reporting.

- Section 8B - *Quarterly reports* provides that the Minister shall submit to the House of Assembly quarterly financial reports on the state of the public finances, and such other financial or economic reports as the Minister determines
- A goal to limit foreign debt to 20% of total public debt has been defined in Section 52A - *Reduction in foreign current borrowings.* The Section also notes that while the foreign exchange exposure remains above 20% there can be no management-induced increase in foreign exchange exposure.
- Section 60A - *Sale of Crown Assets* provides for net sale proceeds to be used to reduce public debt.
- Proposed public financing by crown corporations must be reported to the House of Assembly under Section 73 - *Annual Reports to House of Assembly.*

13.32 Finance has been investigating its management and information systems requirements related to debt management and other treasury management functions. At the time of this update review, a draft request for proposals for the implementation of necessary Treasury Management systems was being considered.

Highlights of Significant Outstanding Issues or Concerns

13.33 From discussions with Finance senior management and a review of information provided, it is evident that considerable action has been taken or is planned. Additional and ongoing effort will be required to fully implement the policies, maintain plans and implement systems necessary to support improved and continued control of the Province's debt and debt-related activities. Certain of the more significant issues which remain to be fully addressed are discussed below.

13.34 Formal reporting to parties external to the ongoing debt management function (e.g., Executive Council, House of Assembly) on Finance's performance, with respect to the *Debt Management Plan* and compliance with policy, needs to be defined and appropriately incorporated into statutory and/or policy accountability reporting requirements.

13.35 Appendix 8B to our 1995 chapter on debt management summarized key governance questions for the use and control of derivatives (adapted from a booklet entitled *Derivatives for Directors*, published by KPMG - one of a number of available references for debt management practices or guidelines). Not all the issues and concerns raised have been fully dealt with, and because they relate to ensuring appropriate governance over the management of the Province's debt and debt-related activities, these should be subject to further consideration.

13.36 The investment and liability management functions are managed by a small number of qualified and experienced staff at Finance. This poses risks to the Province in the event of staff changes. For example the Executive Director, appointed in 1994, was leaving the employ of the Province at the end of 1997. In an attempt to manage and mitigate such risks, an internal committee structure related to debt management has been formally established at Finance (see paragraph 13.28 and Exhibit 13.2(b)). In addition, senior management have indicated that they will contract necessary resources to cover short-term needs. We acknowledge that the committee structure implemented to support the management of the Province's debt may mitigate some, but not all, such risks, particularly in relation to the more complex or technical treasury product considerations.

13.37 Finance indicated efforts are continuing to establish a benchmark portfolio to assist with the debt (and investment) management activities. Further, policies and guidelines (limits, restrictions, mix, etc.) related to the management and monitoring of the Public Debt Retirement Fund and the sinking fund investments need to be formalized. Overall, control of these activities should benefit from the definition of more detailed policies or guidelines and adherence to them.

CONCLUDING REMARKS

13.38 The size of the Province's total debt, together with the proportion payable in foreign currencies, warrants increased reporting to and attention by government and the House of Assembly. The Department of Finance has taken and continues to take action to enhance its policies and practices relating to the ongoing management and control of the Province's debt and related costs.

13.39 There are significant public policy issues and decisions related to the management of the Province's debt such as the appropriate level of debt, the appropriate mix of foreign and domestic debt, and the level of acceptable risk. It is not the role of this Office to actively participate in such discussions. Our role and focus is on whether policies, plans and systems exist and operate to support the overall governance, accountability and management processes regarding the control of the Province's debt and debt-related costs. It is incumbent on government to ensure that sufficient appropriate resources are allocated to achieve the level of management control necessary in the circumstances. Regardless of which public policy direction or emphasis is taken, the management of the Province's debt will most likely continue to be a matter of significance and interest to the House of Assembly.

Exhibit 13.1

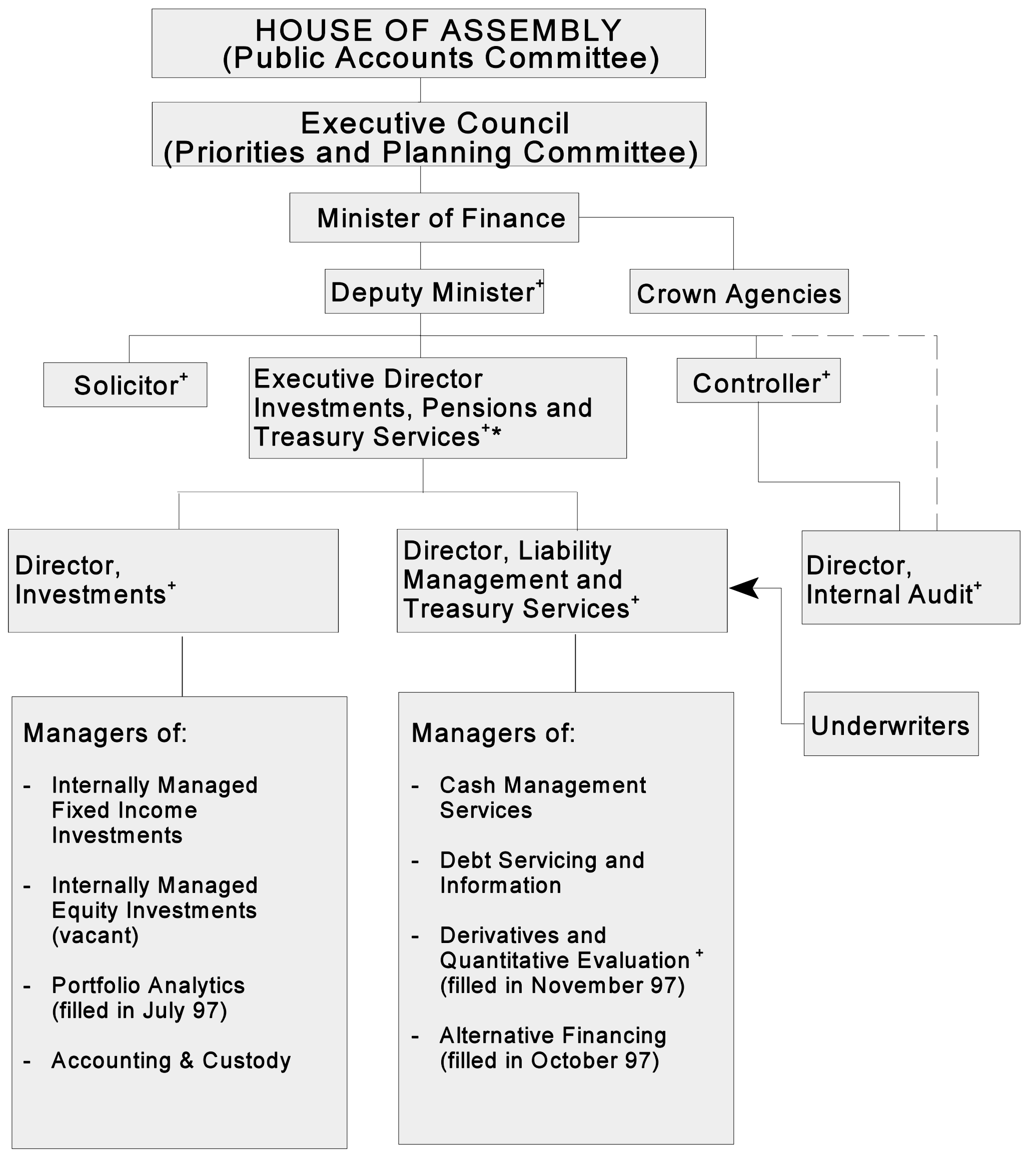
SUMMARY OF PROVINCE'S DEBT
ON MARCH 31, 1997 STATEMENT OF FINANCIAL POSITION
(NON-CONSOLIDATED)

	(thousands of Canadian $)		Foreign %	
	1997	**1996**	**1997**	**1996**
Debentures				
Payable in Canadian Dollars	$ 4,395,558	$ 3,722,811		
Payable in US Dollars	4,002,482	3,759,297		
Payable in Japanese Yen	1,230,900	1,785,000		
Payable in Swiss Francs	240,625	492,866		
Payable in U.K. Pounds	79	187,254		
Other capital liabilities	249,083	302,771		
Bank advances and short-term debt	395,132	428,763		
Commerical Debt	**10,513,859**	**10,678,762**	**57**	**58**
Pension and retirement obligations	866,749	996,780		
Gross Debt (Note A)	**11,380,608**	**11,675,542**	**52**	**53**
Deficiencies in crown corporations (Note C)	463,911	473,067	(Note B)	(Note B)
Total Debt to be Managed	**11,844,519**	**12,148,609**	**54**	**55**
Less:				
Sinking funds				
- debentures	1,552,302	1,316,540	25	23
- other capital liabilities	90,068	102,130		
Public Debt Retirement Fund	709,540	648,346	35	35
Funds to be Managed	**2,351,910**	**2,067,016**	**27**	**25**
Net Debt	**$ 9,492,609**	**$ 10,081,593**	**60**	**61**
Consisting of:				
Net debenture debt	$ 7,607,802	$ 7,982,342	70	71
Net other capital liabilities	159,015	200,641		
Bank advances and short-term	395,132	428,763		
Net Commerical Debt	**8,161,949**	**8,611,746**	**65**	**66**
Pension and retirement obligations	866,749	996,780		
(Note A)	**9,028,698**	**9,608,526**	**59**	**59**
Deficiencies in crown corporations	463,911	473,067	(Note B)	(Note B)
Net Debt	**$ 9,492,609**	**$ 10,081,593**	**60**	**61**

Notes:
A - The *Debt Management Plan* includes debt to this level.
B - Included is the net deficiency of a number of crown corporations. The most significant is Nova Scotia Resources Limited which has issued debt in foreign currency.
C - See note 5 to March 31, 1997 financial statements - Contingent Liabilities and Commitments - for information on debts and obligations of government enterprises guaranteed by the Province but not covered by Finance's current plans.

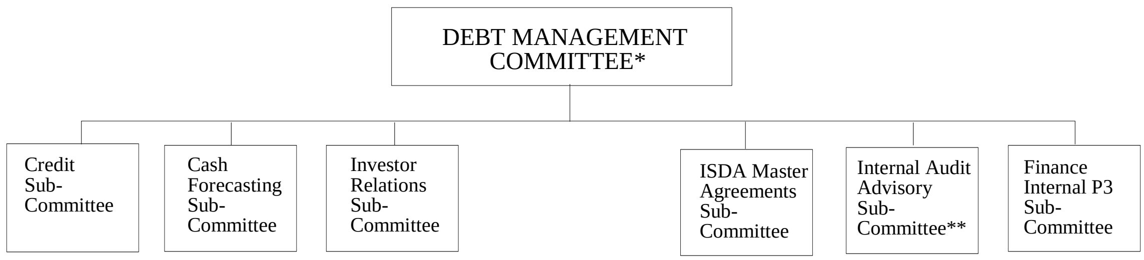
Exhibit 13.2(a)

DEBT MANAGEMENT ORGANIZATION OVERVIEW



+ These positions also serve on Finance's internal Debt Management Committee (chaired by the Deputy Minister) and where appropriate selected sub-committees defined in the draft debt management policy. (See Exhibit 13.2(b)).
* Also has responsibilities for pension services and regulation.

Exhibit 13.2 (b)



* Chaired by Deputy Minister of Finance. For membership see Exhibit 13.2(a)

**Representatives from the Office of the Auditor General and the public accounting firm appointed under Section 65 of the Provincial Finance Act sit as observers on this sub-committee

Exhibit 13.3

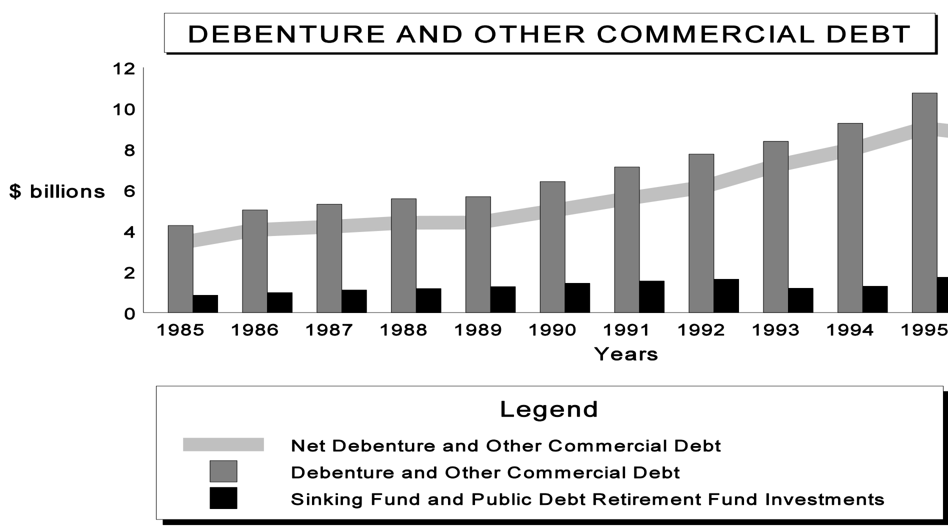


Exhibit 13.4

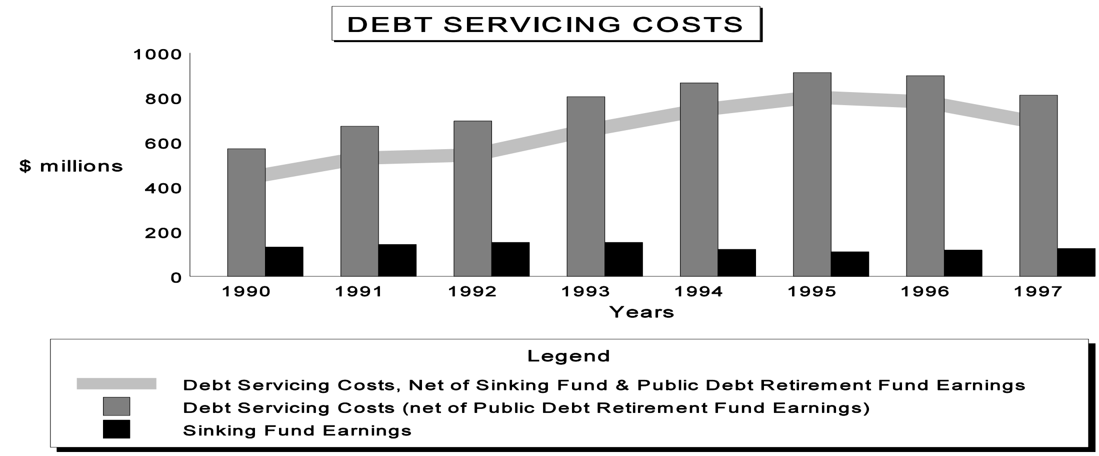


Exhibit 13.5

Foreign Exchange Exposure*
as at March 31
(millions of Canadian $)

	1990	**1991**	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**
Foreign Debt (Gross)	$ 3,366	$ 4,187	$ 4,488	$ 4,882	$ 5,925	$ 7,554	$ 6,224	$ 5,951
Percent of gross debt	50%	57%	57%	55%	59%	64%	53%	52%
Foreign Debt (Net)	$ 2,638	$ 3,360	$ 3,660	$ 4,624	$ 5,632	$ 7,115	$ 5,702	$ 5,324
Percentage of net debt	50%	57%	58%	61%	64%	71%	59%	59%

*Excluding foreign debt of crown corporations

CROWN AGENCIES AND CORPORATIONS

14.

ATLANTIC LOTTERY CORPORATION INC. - FOLLOW-UP OF 1996 SHAREHOLDER'S AUDIT

BACKGROUND

14.1 Our Report last year included a chapter on the results of our audit coverage of the Atlantic Lottery Corporation Inc. (ALC). That audit was requested under the Shareholder's Audit provision of ALC's Corporate bylaws by the Nova Scotia Gaming Corporation (NSGC), in its capacity as the Nova Scotia shareholder.

14.2 ALC was incorporated in 1976 under the Canada Business Corporations Act, and is jointly and equally owned by the Atlantic provinces. Since being established, ALC has reported sales in excess of $5.5 billion up to and including the fiscal year ended March 31, 1997. After prizes, commissions and other costs of approximately $3.6 billion, ALC has distributed profits of $1.85 billion to its shareholders, including $733.8 million to Nova Scotia. On behalf of its four shareholders ALC is now directly involved in the annual management and control of more than $1 billion of public funds through its various gaming products and related activities.

14.3 The original enabling inter-provincial agreements signed in 1976 provided the following with respect to the mandate or purpose for the Corporation.

> *"The Atlantic Lottery Corporation, a body corporate incorporated under the Canada Business Corporations Act, is designated as and hereby becomes an agency of Her Majesty in the right of* [each of the shareholder provinces] *for the purpose of conducting and managing lottery schemes in each of those Provinces or other Provinces."*

14.4 In the fall of 1997, subsequent to ALC management's appearance before the Nova Scotia Legislature's Public Accounts Committee (PAC), we requested information from ALC on the status of action taken or planned for the specific recommendations included in our Report as a result of the 1996 Shareholder's Audit. Since certain of the recommendations in that report required shareholder involvement, we also sought information from the NSGC.

14.5 The purpose of this chapter is to provide current information on ALC, the status of action taken or planned, and summary observations resulting from our follow-up.

RESULTS IN BRIEF

14.6 The following highlights the principal observations from our review.

- Since last year's Report, progress has been made in implementing the recommendations. There still remains much to accomplish, particularly with regard to matters requiring agreement of the shareholders.

- The manner in which ALC's costs and profit are being allocated continues to result in certain shareholder provinces, in essence, subsidizing other jurisdictions. During the audit in 1996, by applying an alternative cost allocation methodology to ALC's 1995-96 results, we estimated that Nova Scotia's share of ALC's profit distribution could have been higher. Similar impacts could be anticipated each year until the issue is resolved.

- ALC's status as an agency of government has yet to be resolved. This matter should be clarified, and the applicability to its operations of the various and differing statutory and other administrative policy directives (e.g., wage restraint, expenditure control) in the shareholder provinces needs to be determined. ALC's status as a Nova Scotia crown corporation has been resolved. It is not a Nova Scotia crown corporation under various Nova Scotia statutes.

SCOPE OF REVIEW

14.7 The objective of this review was to determine the action taken or planned by ALC and its shareholders related to the management and control of certain aspects of the Corporation's operations. We also wanted to provide updated background information and analysis on ALC and the results of its operations in order to support increased awareness and understanding.

14.8 Our approach included discussions with ALC and NSGC representatives, and a review of available documentation, including ALC's Board and Audit Committee minutes, ALC's Annual Report and testimony to the PAC in Nova Scotia.

14.9 We have not performed specific audit verification of the various representations provided to us, and provide no opinion on their completeness and accuracy.

PRINCIPAL FINDINGS

Updated Background Information

14.10 Each of the Atlantic provinces has lottery and gaming related statutes in place, with supporting regulations, that must be appropriately considered and complied with by ALC. While similar, there are some regulatory or policy directive differences (e.g., regarding video lottery terminals). Historically, ALC has played a role in the monitoring of regulatory compliance for each jurisdiction. Various inter-provincial agreements have been signed with respect to ALC. Further, ALC has Corporate bylaws, last updated and approved by the Corporation's Board of Directors and the shareholder provinces in 1994. These lay out the basic framework under which ALC's Board and management must function.

14.11 Each shareholder province can appoint two representatives to an eight member Board of Directors, and each shareholder has one of its Board representatives on the Corporation's audit committee. Decisions are usually determined based upon a majority vote, except where a decision affects only one province. Another exception is changes to the methodology for allocation of profits to the shareholders, which require unanimous approval.

14.12 Each shareholder province also holds a share in and has one representative on the Board of Directors of the Inter-Provincial Lottery Corporation (ILC). The ILC coordinates and manages the national lottery programs through "regional marketing organizations." ALC is the regional marketing organization for Atlantic Canada, and must adhere to defined policies and standards for national lottery games (e.g., 6/49, super 7).

14.13 Last year's chapter included a significant amount of background information and analysis on ALC's organization and results. We have reproduced the following exhibits, most of which were included in last year's report, updated to reflect 1997 organizational changes, plans and operating results to March 31, 1997:

Exhibit 14.1 - Overall Governance, Accountability and Management Organization in 1997

Exhibit 14.2 - Corporate Mission and Key Objectives

Exhibit 14.3 - Summary of Results

Exhibit 14.4 - Summary of Operating Expenses

Exhibit 14.5 - Summary of Terminals and Sites

Exhibit 14.6 - Allocation of Gross Profit by Game Type

Exhibit 14.7 - Income from Video Lottery

Exhibit 14.8 - Video Lottery Receipts

Exhibit 14.9 - Profits Distributed

14.14 ***Organization Overview*** - ALC, through its Board of Directors, has operational and regulatory accountability relationships to each of the Atlantic provinces. Exhibit 14.1 on page 149 provides summary information on the governance, accountability and management organization for ALC's operations during 1997.

14.15 ***Corporate Mission and Key Objectives*** - ALC's response to our request for information on the status of action taken or planned indicates that a new Corporate strategic plan was approved by the Board on October 6, 1997. Exhibit 14.2 on page 150 includes ALC's updated mission statement and a summary of the Corporation's key objectives and related measures defined in the strategic plan. It is our understanding that the key objectives will be subject to further Board discussions.

14.16 ***Summary of ALC's Results*** - Exhibit 14.3 on page 151 provides information from ALC's *Statement of Operations and Allocation of Profit* over the last five years and in total for the life of the Corporation. It shows ALC has two main sources of revenue, the "Net video lottery receipts" from the video lottery program (VLP) and the "Gross ticket sales" from all other lottery programs.

14.17 ***Financial Control and Reporting*** - ALC's audited financial statements are presented to the Board and published in the Corporation's Annual Report. Exhibit 14.4 on page 152 provides a summary of the operating expenses by division, for the period 1993 to 1997, as reported in the audited financial statements. We have included an alternative break down of the operating expenses by category which is not disclosed in the audited financial statements.

14.18 ***Video Lottery Program (VLP)*** - Since the implementation of VLP in 1990-91, the video lottery program has been and is the fastest growing of ALC's gaming programs. There are differences in how the program is regulated and resourced by the individual shareholder provinces. The VLP has been the subject of significant public interest, and concerns have been raised in the past about the adequacy of the information and reporting on the program's activities and results. The following comments and information on the VLP provide an indication of both the significance of the program and the need for improved information and reporting of ALC's plans and results with respect to it.

14.19 *Summary of terminals and sites* - Exhibit 14.5 on page 153 includes information on the results, sites and commissions related to the VLP in comparison to the regular lottery activities for the year ended March 31, 1997.

14.20 *Allocation of gross profit by game type* - Exhibit 14.6 on page 154 categorizes the direct expenses from the financial statements under the headings "Video Lottery" and "Ticket Games" to determine a gross profit by game type. The exhibit illustrates the significant growth of the VLP with respect to its contribution to the gross profit of ALC. The VLP contribution to gross profit in 1994 was approximately 77% of the amount generated from ticket games. Three years later in 1997 the VLP gross profit is 115% of the amount generated from ticket games. Since 1994, the VLP's contribution to gross profit had increased 77% from $109 million to $193 million. Ticket games' gross profit grew from $142 million to $167 million, an increase of about 18% during the same period.

14.21 *Income from video lottery* - Exhibit 14.7 on page 155 provides the net video lottery receipts and the related expenses for each shareholder province for the year ended March 31, 1997. New Brunswick and Prince Edward Island have involved third-party private sector coin-operators in carrying out the video lottery program. ALC has operated this program for Nova Scotia and Newfoundland without the involvement of private sector coin-operators.

14.22 *Compliance with VLT prize payout regulations* - Financial information was obtained from ALC to enable the preparation of a schedule showing "cash in" and "cash out" (which prior to 1995-96 were termed "gross video lottery receipts" and "prize expense"), and the resulting net video lottery receipts, which agreed with the financial statements of ALC. Results for the last four years are shown in Exhibit 14.8 on page 156.

14.23 ***Segmented Operations by Province*** - ALC's annual report at March 31, 1997, page 22, included a summary of the results of segmented operations by province which shows the contributions that traditional and video lottery make to gross profit. These contributions were determined on the basis of the current profit allocation methodology and are not determined on a full cost basis. Management have indicated that this information will be provided on a more full cost basis in ALC's 1997-98 annual report. We have prepared Exhibit 14.9 on page 157, which provides a more detailed segmented analysis of the results for 1996-97 for ALC in total and Nova Scotia's share.

Status of Action Taken or Planned

14.24 During the course of last year's audit, we identified opportunities to improve the level of control and reporting in selected areas. Our report to the Nova Scotia Gaming Corporation as a result of the 1996 Shareholder's Audit included various recommendations for consideration by the appropriate combination of ALC's management, Board, shareholders and/or shareholder provinces.

14.25 As part of this follow-up review process we requested ALC and the Nova Scotia shareholder to provide us with summary representations of the status of action taken or planned in relation to the recommendations included in last year's Report. Appendix 14A to this chapter on page 158 lists our recommendations, organized under the major headings of last year's Report, together with the status comments received from ALC and the NSGC. ALC's initial response included in last year's chapter is entitled ALC 96, and the Corporation's responses during 1997 are titled ALC July/97 and ALC Nov/97 Update. The NSGC's comments are italicized, and are provided for those recommendations that required consideration by shareholders directly.

Discussion of Significant Issues

14.26 ***Profit Distribution*** - The unanimous shareholder agreement, of November 15, 1976 and amended April 8, 1991, dictates the manner in which ALC's costs and profit are to be allocated and results in certain shareholder provinces, in essence, subsidizing other jurisdictions. We acknowledge that action has commenced to correct this situation, with the NSGC's introduction of a motion to amend the profit allocation formula at the ALC shareholder meeting held on June 16, 1997.

14.27 Using information for the 1995-96 fiscal year, we estimated that Nova Scotia's share of ALC's profit distribution could have been higher in that year if a fuller and fairer allocation of costs had been part of the approved profit distribution methodology. Similar impacts could be anticipated each year until the profit distribution methodology is revised.

14.28 Further, the impact on profit distributions of the Board's decisions to enter into a long-term lease for the new head office space and the new retail terminal project will commence with the fiscal year ended March 31, 1998.

14.29 ***ALC's Status*** - This has been a topic of significant research and discussion, and is yet to be resolved. We note that the focus has tended to be limited to ALC's status as a "crown corporation". It has been indicated that ALC is not a crown corporation under Section 70 of the Provincial Finance Act. However, we wish to emphasize that in Nova Scotia there are other categories or classifications for public sector entities that need to be considered as well (e.g., *"agency of government"* as defined in Section 2(1)(a) of the Auditor General Act, which is referred to in other statutes such as the Public Sector Compensation (1994-1997) Act; and *"department"* as defined in Section 2(e) of the Provincial Finance Act). Further, ALC's status needs to be formally clarified in order to determine the applicability to its operations of the various and differing statutory and administrative policy directives of the shareholder provinces.

14.30 ***Wage Restraint*** - During ALC management's meeting with the Nova Scotia PAC on October 15, 1997, information was requested on recent year's compensation changes (i.e., economic and merit). In response to the inquiries by Committee Members, ALC management focussed solely on the data that was included in our 1996 Report. ALC management did not indicate to the PAC that the Corporation's Board had approved additional compensation increases that took affect in 1997-98. ALC's Board minutes of May and June 1997 indicate that economic and other increases to management and staff were approved for 1997-98. We raise this point as it relates to ALC's status as an *"agency of government"* under the Auditor General Act, a definition that is referred to directly in the applicability of the Public Sector Compensation (1994-1997) Act in Nova Scotia.

14.31 ***ALC's Annual Report*** - Some of our recommendations to expand and improve ALC's Annual Report have been implemented, resulting in improved reporting for the year ended March 31, 1997. ALC's Annual Report included a number of representations. We wish to draw attention to the representation *"We were pleased, though not surprised, when the report confirmed that ALC is a credible, accountable organization."* (included on page 9 of ALC's Annual Report), which related to the shareholder's audit conducted jointly by the Auditors General of Nova Scotia and New Brunswick. This statement is not consistent with the overall conclusion resulting from the review and our Report clearly identifies the need for improved accountability and reporting by ALC.

CONCLUDING REMARKS

14.32 Action has been taken, or is in process or planned by ALC and its shareholders, to deal with many of the recommendations included in last year's Report. However, there remain significant issues to be fully dealt with by ALC and its shareholders, including those impacting on the economy and efficiency of ALC's activities and results as they relate to gaming in Nova Scotia.

Exhibit 14.1

Overall Governance, Accountability and Management Organization in 1997

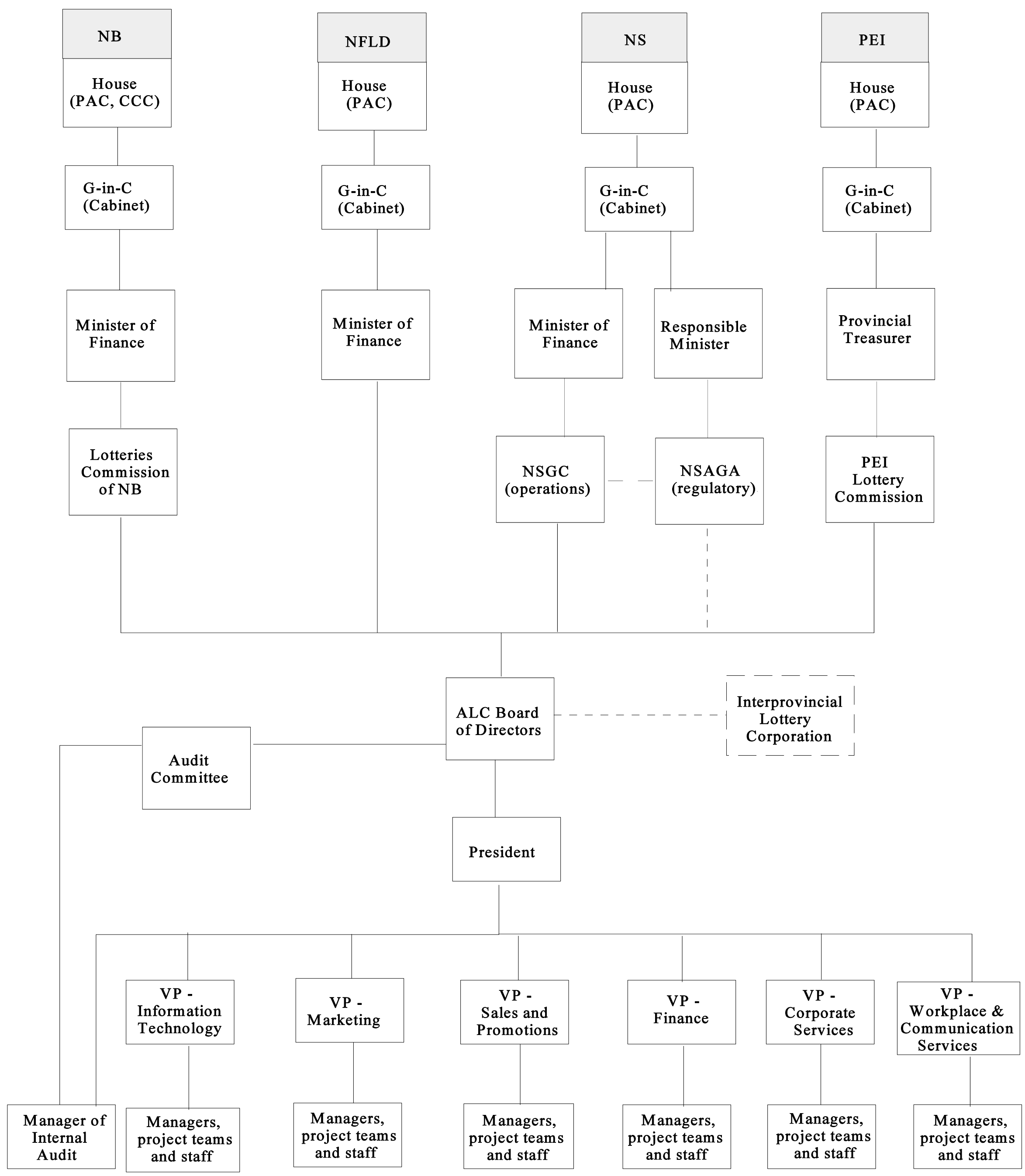


Exhibit 14.2

CORPORATE MISSION AND KEY OBJECTIVES
(Source: ALC's 1997-2001 Strategic Plan)

Mission

"The ALC is committed to being the shareholders' agency of choice by managing profitable, entertaining lottery and gaming activities within the existing social and legal framework in Atlantic Canada."

Key Objectives	To be Measured By
To achieve targeted growth through maintenance of existing products, development of new products and expansion into new channels of distribution.	- *Revenue and profit growth* - *Percentage of growth from new products and new channels*
To continually improve on ALC's efficiency, effectiveness and profit.	- *Revenue and profit per employee* - *Operating costs in comparison to other lotteries*
To continually improve on ALC's asset utilization.	- *Profit per terminal* - *Rate of return on investment in new technology*
To enhance shareholder relations.	- *Shareholder satisfaction*
To provide players with products that are enjoyable to play and conveniently available.	- *Customer satisfaction with ALC products and retailer service* - *Players as a percentage of adult population*
To provide our retailers with the service and support they require to give the best possible service to our players.	- *Retailer satisfaction* - *Product availability*
To be recognized as a responsible, trustworthy and innovative corporation.	- *Public approval ratings* - *Media tracking scores*
To ensure that internal processes meet changing customer needs.	- *Availability of gaming and business systems* - *Percentage of sales from new products* - *New product introduction versus other lotteries*
To foster a satisfying, challenging and motivating work environment with appropriate work tools and information that results in productive and contributing employees.	- *Employee satisfaction (Work Environment Survey)* - *Employee turnover*

Exhibit 14.3

Summary of Results as at March 31 ($000)

(Source: ALC's audited and internal financial statements)

	Total	1997	1996	1995	1994	1993	Sub-total 1976 to 1992
Sales:							
Gross ticket sales	$4,184,887	$ 454,244	$ 436,781	$ 409,406	$ 370,037	$ 346,995	$2,167,424
Net video lottery receipts	1,301,507	299,947	281,047	246,507	195,493	183,897	94,616
	5,486,394	754,191	717,828	655,913	565,530	530,892	2,262,040
Direct expenses:							
Prizes on ticket sales	2,107,311	243,239	233,035	216,014	193,295	180,665	1,041,063
Commissions	801,896	139,738	131,708	122,805	112,357	111,724	183,565
- Regular lottery	383,723	32,922	31,916	29,335	26,380	24,686	131,668
- VLT site-holders	286,124	75,681	70,919	64,303	59,773	60,153	30,976
- VLT owners (coin operators)	132,049	31,135	28,873	29,166	26,204	26,885	20,921
Ticket printing	119,382	10,938	9,461	9,272	8,318	9,092	72,301
	3,028,585	393,915	374,204	348,091	313,970	301,481	1,296,929
Gross profit	2,457,805	360,276	343,624	307,822	251,561	229,411	965,111
Operating expenses	497,365	54,666	51,325	51,079	42,012	40,676	257,607
Operating profit	1,960,440	305,610	292,299	256,743	209,548	188,735	707,504
Interest and other income	25,658	2,392	2,852	886	645	989	17,894
	1,986,098	308,002	295,151	257,629	210,194	189,724	725,398
Less:							
- Government of Canada	56,434	3,635	3,565	3,525	3,584	3,444	38,681
- Goods and Services Tax	65,368	13,116	11,970	11,250	9,549	11,319	8,164
- Special commissions to non-profit organizations	3,781	209	220	260	254	302	2,536
- NS retailers bonus	10,483	3,936	3,733	2,814	-	-	-
	136,066	20,896	19,488	17,849	13,387	15,065	49,381
Profit available for distribution	$1,850,032	$ 287,106	$ 275,663	$ 239,781	$ 196,806	$ 174,659	$ 676,017
Profit allocation:							
New Brunswick	$ 559,602	$ 87,026	$ 82,031	$ 63,902	$ 57,412	$ 47,236	$ 221,995
Newfoundland	458,659	75,038	74,117	69,173	54,627	43,664	142,040
Nova Scotia	733,852	110,243	104,916	94,055	73,320	75,266	276,051
Prince Edward Island	97,919	14,799	14,599	12,650	11,447	8,493	35,931
	$1,850,032	$ 287,106	$ 275,663	$ 239,781	$ 196,806	$ 174,659	$ 676,017

Exhibit 14.4

Summary of Operating Expenses ($000)
(Source: ALC's audited and internal financial statements)

	1997		1996		1995		1994		1993	
Expense by Division, Per Financial Statements										
Marketing	$ 9,055	16.6%	$ 8,694	16.9%	$ 8,757	17.1%	$ 5,230	12.4%	$ 6,394	15.7%
Sales and Promotion	8,226	15.0%	7,601	14.8%	7,984	15.6%	7,028	16.7%	6,658	16.4%
Finance	2,318	4.2%	2,108	4.1%	2,058	4.0%	2,048	4.9%	1,760	4.3%
Corporate Services	8,238	15.1%	7,511	14.7%	7,218	14.1%	6,334	15.1%	6,667	16.4%
Information Systems	26,829	49.1%	25,412	49.5%	25,062	49.1%	21,372	50.9%	19,197	47.2%
Total	$ 54,666	100.0%	$ 51,325	100.0%	$ 51,079	100.0%	$ 42,012	100.0%	$ 40,676	100.0%
Expense by Category										
Salaries & benefits	$ 16,622	30.4%	$ 15,391	30.0%	$ 14,175	27.8%	$ 12,242	29.1%	$ 11,226	27.6%
Depreciation	9,504	17.4%	9,649	18.8%	9,890	19.4%	9,422	22.4%	8,042	19.8%
Advertising	6,500	11.9%	5,962	11.6%	6,277	12.3%	3,673	8.7%	5,275	13.0%
Market development	897	1.6%	998	1.9%	991	1.9%	824	2.0%	461	1.1%
Communication material	553	1.0%	656	1.3%	543	1.1%	509	1.2%	665	1.6%
General services	2,233	4.1%	2,214	4.3%	2,356	4.6%	1,581	3.8%	0	0.0%
Professional services	209	0.4%	180	0.4%	173	0.3%	279	0.7%	2,345	5.8%
Occupancy cost	1,813	3.3%	1,438	2.8%	1,618	3.2%	1,334	3.2%	1,220	3.0%
Office supplies	526	1.0%	510	1.0%	678	1.3%	879	2.1%	788	1.9%
Vehicle leasing	359	0.7%	56	0.1%	0	0.0%	0	0.0%	0	0.0%
Rent of equipment	84	0.2%	74	0.1%	133	0.3%	139	0.3%	218	0.5%
Equipment & maintenance	3,757	6.9%	3,598	7.0%	3,528	6.9%	2,315	5.5%	2,839	7.0%
Telecommunications	5,977	10.9%	5,545	10.8%	4,943	9.7%	4,358	10.4%	3,830	9.4%
Travel & vehicle	1,993	3.7%	1,867	3.6%	1,775	3.5%	1,655	3.9%	1,750	4.3%
Retail sales support	2,128	3.9%	1,808	3.5%	2,184	4.3%	1,267	3.0%	879	2.2%
Human resources	267	0.5%	185	0.4%	346	0.7%	316	0.8%	124	0.3%
Training	377	0.7%	327	0.6%	330	0.6%	428	1.0%	218	0.5%
Bad debt	92	0.2%	100	0.2%	234	0.5%	102	0.2%	170	0.4%
Other	775	1.4%	767	1.5%	905	1.8%	689	1.6%	626	1.5%
Total	$ 54,666	100.0%	$ 51,325	100.0%	$ 51,079	100.0%	$ 42,012	100.0%	$ 40,676	100.0%

Exhibit 14.5

Summary of Terminals and Sites
For the Year Ended March 31, 1997
(Source: ALC & ALC's internal financial statements)

	Total	NB	Nfld	NS	PEI
Regular Lottery					
Gross Sales	$ 454,244,000	$ 109,650,000	$ 147,434,000	$ 172,652,000	$ 24,508,000
Retailer Commissions*	$ 36,858,000	$ 8,280,000	$ 9,865,000	$ 16,850,000	$ 1,863,000
Average Number of On-Line Terminals	3,228	844	1,107	1,125	153
Average per On-line Terminal					
- Gross Sales	$ 140,720	$ 129,917	$ 133,183	$ 153,469	$ 160,187
- Retailer Commissions	$ 11,418	$ 9,810	$ 8,911	$ 14,978	$ 12,176
Video Lottery					
Total Cash In	$ 923,558,000	$ 287,971,000	$ 222,802,000	$ 374,307,000	$ 38,478,000
Net VLT Receipts (Net Sales)	$ 299,947,000	$ 116,274,000	$ 60,793,000	$ 106,007,000	$ 16,873,000
Siteholder Commission	$ 75,681,000	$ 27,156,000	$ 15,151,000	$ 29,396,000	$ 3,978,000
Average Number of VLTs	9,623	3,728	2,240	3,026	629
Average Number of Siteholders	2,932	1,614	491	585	242
Average Cash In					
- Per VLT	$ 95,974	$ 77,245	$ 99,465	$ 123,697	$ 61,173
- Per Site	$ 314,992	$ 178,421	$ 453,772	$ 639,841	$ 159,000
Average Net VL Receipts (Net Sales)					
- Per VLT	$ 31,170	$ 31,189	$ 27,140	$ 35,032	$ 26,825
- Per Site	$ 102,301	$ 72,041	$ 123,815	$ 181,209	$ 69,723
Average Siteholder Commission					
- Per VLT	$ 7,865	$ 7,284	$ 6,764	$ 9,714	$ 6,324
- Per Site	$ 25,812	$ 16,825	$ 30,857	$ 50,249	$ 16,438

*Includes Nova Scotia Bonus Commission of $3,936,000

Exhibit 14.6

Allocation of Gross Profit by Game Type ($000)
(Source: ALC & ALC's external auditor)

	1997			1996		
	Video Lottery	**Ticket Games**	**Total**	**Video Lottery**	**Ticket Games**	**Total**
Gross ticket sales	$ -	$ 454,244	$ 454,244	$ -	$ 436,780	$ 436,780
Net video lottery receipts	299,947	-	299,947	281,047	-	281,047
	299,947	454,244	754,191	281,047	436,780	717,827
Direct expenses						
Prizes on ticket sales	-	243,239	243,239	-	233,035	233,035
Commissions*	106,816	32,922	139,738	99,792	31,915	131,707
Ticket printing	253	10,685	10,938	231	9,230	9,461
	107,069	286,846	393,915	100,023	274,180	374,203
Gross profit	$ 192,878	$ 167,398	$ 360,276	$ 181,024	$ 162,600	$ 343,624
	54%	46%	100%	53%	47%	100%

	1995			1994		
	Video Lottery	**Ticket Games**	**Total**	**Video Lottery**	**Ticket Games**	**Total**
Gross ticket sales	$ -	$ 409,406	$ 409,406	$ -	$ 370,037	$ 370,037
Net video lottery receipts	246,507	-	246,507	195,493	-	195,493
	246,507	409,406	655,913	195,493	370,037	565,530
Direct expenses						
Prizes on ticket sales	-	216,014	216,014	-	193,295	193,295
Commissions*	93,469	29,336	122,805	85,976	26,380	112,356
Ticket printing	137	9,135	9,272	158	8,160	8,318
	93,606	254,485	348,091	86,134	227,835	313,969
Gross profit	$ 152,901	$ 154,921	$ 307,822	$ 109,359	$ 142,202	$ 251,561
	50%	50%	100%	43%	57%	100%

*Excludes Nova Scotia Bonus Commissions of 1997 - $3,936; 1996 - $3,733; 1995 - $2,814 and 1994 - $0

Exhibit 14.7

Income from Video Lottery
For the Year Ended March 31, 1997 ($000)
(Source: ALC & ALC's external auditor)

	Total	N.B.		P.E.I.		N.S.		Nfld.	
			%		%		%		%
Net video lottery receipts	$ 299,947	$ 116,274	100	$ 16,873	100	$ 106,007	100	$ 60,793	100
Direct costs									
Retailer commission	75,682	27,157	23.35	3,978	23.57	29,396	27.73	15,151	24.92
Coin-operator commission	31,134	27,156	23.35	3,978	23.57				
Ticket costs	253					161	0.15	92	0.15
Gross profit	192,878	61,961	53.29	8,917	52.85	76,450	72.12	45,550	74.92
Operating expenses									
Salaries and benefits	1,577					804	0.76	773	1.27
Depreciation - vehicles	111					63	0.06	48	0.08
Depreciation - terminals	5,777					3,626	3.42	2,151	3.54
Terminal movement	1					1	0.00	-	0.00
Occupancy costs	198					78	0.07	120	0.20
Vehicle leasing	94					47	0.04	47	0.08
Equipment & maintenance	573					335	0.32	238	0.39
Video lottery software	432					274	0.26	158	0.26
Vehicles and travel	298					123	0.12	175	0.29
Bad debts	33					13	0.01	20	0.03
Meetings	2					1	0.00	1	0.00
Financing	452					243	0.23	209	0.34
GST	7,842	3,824	3.29	481	2.85	2,276	2.15	1,261	2.07
Terminal write offs	(69)					1	0.00	(70)	(0.11)
Administrative recovery	(595)					(595)	(0.56)	-	0.00
Total operating expenses	16,726	3,824	3.29	481	2.85	7,290	6.88	5,131	8.44
Income from video lottery	$ 176,152	$ 58,137	50.00	$ 8,436	50.00	$ 69,160	65.24	$ 40,419	66.49

Note: Shaded areas represent jurisdictions using coin operators.

Exhibit 14.8

Video Lottery Receipts ($000)
(Source: ALC & ALC's external auditor)

	New Brunswick		Prince Edward Island		Nova Scotia		Newfoundland		Total	
	$	%	$	%	$	%	$	%	$	%
1996 - 1997										
Cash In	287,971	100.0	38,478	100.0	374,307	100.0	222,802	100.0	923,558	100.0
Cash Out	171,697	59.6	21,605	56.1	268,300	71.7	162,009	72.7	623,611	67.5
Net Sales	116,274	40.4	16,873	43.9	106,007	28.3	60,793	27.3	299,947	32.5
1995 - 1996										
Cash In	254,204	100.0	36,001	100.0	345,992	100.0	202,495	100.0	838,692	100.0
Cash Out	146,904	57.8	19,825	55.1	246,809	71.3	144,107	71.2	557,645	66.5
Net Sales	107,300	42.2	16,176	44.9	99,183	28.7	58,388	28.8	281,047	33.5
1994 - 1995										
Gross Video Lottery receipts	211,718	100.0	32,659	100.0	311,006	100.0	160,918	100.0	716,301	100.0
Prize Expense	120,020	56.7	17,936	54.9	220,646	70.9	111,192	69.1	469,794	65.6
Net Video Lottery Receipts	91,698	43.3	14,723	45.1	90,360	29.1	49,726	30.9	246,507	34.4
1993 - 1994										
Gross Video Lottery receipts	180,093	100.0	31,152	100.0	225,350	100.0	117,272	100.0	553,867	100.0
Prize Expense	100,286	55.7	17,755	57.0	160,585	71.3	79,748	68.0	358,374	64.7
Net Video Lottery Receipts	79,807	44.3	13,397	43.0	64,765	28.7	37,524	32.0	195,493	35.3
Totals - four years										
	933,986	100.0	138,290	100.0	1,256,655	100.0	703,487	100.0	3,032,418	100.0
	538,907	57.7	77,121	55.8	896,340	71.3	497,056	70.7	2,009,424	66.3
Net Video Lottery Receipts	395,079	42.3	61,169	44.2	360,315	28.7	206,431	29.3	1,022,994	33.7

Exhibit 14.9

Profits Distributed
Year Ended March 31, 1997 ($000)
(Source: ALC's audited and internal financial statements)

Atlantic Lottery Corporation	Regular Lottery	%	Video Lottery	Total
Sales				
Gross ticket sales	$ 454,244		$ -	$ 454,244
Net video lottery receipts	-		299,947	299,947
	454,244		299,947	754,191
Prizes on ticket sales	243,239		-	243,239
Net Sales	211,005	100	299,947	510,952
Allocated expenses				
Commissions	32,922		106,816	139,738
Ticket printing	10,685		253	10,938
Operating expenses	45,188		9,478	54,666
Interest and other income	(1,797)		(595)	(2,392)
Payments to Government of Canada	3,635		-	3,635
Goods and Services Tax	5,273		7,843	13,116
	95,906	100	123,795	219,701
Special commissions to non-profit organizations	209		-	209
Nova Scotia retailer bonus	3,936		-	3,936
Total allocated expenses	100,051		123,795	223,846
Profit distributed to shareholders	$ 110,954	100	$ 176,152	$ 287,106

Nova Scotia Share	Regular Lottery	%	Video Lottery	Total
Sales				
Gross ticket sales	$ 172,652		$ -	$ 172,652
Net video lottery receipts	-		106,007	106,007
	172,652		106,007	278,659
Prizes on ticket sales	89,966		-	89,966
Net Sales	82,686	39.2	106,007	188,693
Allocated expenses				
Commissions	12,914		29,396	42,310
Ticket printing	4,193		161	4,354
Operating expenses and distributions (net)	20,471		7,290	27,761
	37,578	39.2	36,847	74,425
Special commissions to non-profit organizations	89		-	89
Nova Scotia retailer bonus	3,936		-	3,936
Total allocated expenses	41,603		36,847	78,450
Profit distributed to Nova Scotia	$ 41,083	37.0	$ 69,160	$ 110,243

Appendix 14A

ATLANTIC LOTTERY CORPORATION - FOLLOW-UP REVIEW OF 1996 SHAREHOLDER'S AUDIT

Recommendations for Consideration	Status of Action Taken or Planned
Compliance with Statutory and Policy Requirements 1. The applicability to ALC operations of the various and differing statutory and other administrative policy directives in the shareholder provinces needs to be determined.	**ALC 96** - ALC believes it is in compliance with shareholder provincial requirements. ALC responds in a timely fashion to any information requests or directives from shareholders. **ALC July/97** - None required, except to respond to shareholder directives and information requests. ***NSGC 97*** - *Where policies of the four shareholder provinces are the same, the policies are followed by ALC, for example the Atlantic Procurement Agreement. Where differences exist they are reviewed on a case by case basis.*
Inter-Provincial Agreements 2. The provisions of the inter-provincial agreements should be subject to review and updating to ensure an appropriate and modern governance and accountability framework and process are in place for ALC. Among other matters, this should include consideration of the following: - establishing a set of guiding principles or values to support the interpretation and implementation of the agreements; - establishing the obligation to provide sufficient and appropriate accountability information and reporting to the Legislature in each shareholder province on the Corporation's financial and program plans and performance; - changes necessary to the profit distribution methodology in order to ensure the allocation of costs and results are fair and equitable; and - sunset clauses on selected aspects of the arrangements, so that they will be subject to periodic review and updating.	**ALC 96** - We accept your observations. The ALC shareholders and Board are constantly aware of changing situations. ALC's shareholders have reviewed and revised the profit sharing formula from time to time and recognize that it is timely to do so once again. ALC intends to issue an RFP for the conduct of an economic benefit study in the near future. **ALC July/97** - Profit distribution methodology based on Nova Scotia's proposal is being reviewed with board members. An independent economic benefit study, to include a review of profit distribution methodology, will be conducted. RFP award is planned for May 1997 with report by late August 1997. The strategic planning process commenced in fall 1996 and continues to date with Board reporting by August 25, 1997. **ALC Nov/97 Update** - The Board and Shareholders continue to deal with profit distribution methodologies. Economic Benefit Study has been received. Additional information is being prepared. The Strategic Plan was presented to and approved at the October 6, 1997 Board meeting. ***NSGC 97*** - *NSGC has undertaken a full review of corporate governance issues related to ALC, including NSGC's role as a shareholder of ALC and ALC's role as agent for NSGC. This includes a review of all agreements, bylaws and relevant statutes and regulations.*

Recommendations for Consideration	Status of Action Taken or Planned
2. (Continued)	*ALC has improved information and reporting in 1997 and continues to evaluate further disclosure for 1998. Also, NSGC's annual and quarterly financial statements, which are tabled in the legislature, are more detailed than ALC's.* *Changes to the profit distribution methodology were proposed by NSGC at the June 16, 1997, ALC shareholder meeting. A decision has yet to be made on this issue although further discussions are upcoming.*
3. ALC's status as a crown agency should be formally determined and clarified, both for accountability purposes, and also as to its responsibility to comply with the various statutory and other administrative policy directives in the shareholder provinces.	**ALC 96** - ALC is federally incorporated and each of the four Atlantic provinces own one share. ALC believes this method was followed to demonstrate Atlantic provincial cooperation. **ALC July/97** - None required, except to respond to shareholder directives and information requests. ALC is currently aware of at least three decisions that state that ALC is NOT a crown corporation. These are: - Freedom of Information Act - Official Languages Act - Pension Benefits Act **ALC Nov/97 Update** - Draft memorandum of ALC counsel requested by Board at October 6, 1997 meeting. ***NSGC 97*** *- The definition of a crown corporation depends on each province's specific legislation.* *NSGC has requested its own counsel to advise on the legal status of ALC under Nova Scotia law and has requested that ALC counsel also review the issue.*
Corporate Mission 4. As part of the review and updating of ALC's strategic plans, its mission statement should be interpreted, including appropriate clarification or segregation of the fiscal, societal and other aspects inherent/implicit in the mandate and mission of the Corporation.	**ALC 96** - The ALC strategic plan is being updated. ALC is certainly conscious of societal issues; however, these issues remain in the domain of the shareholder provinces. Agree this should be evaluated. **ALC July/97** - The ALC strategic plan is being updated. Board reporting is planned for August 25, 1997. **ALC Nov/97 Update** - The ALC Strategic Plan was approved by the Board October 6, 1997.
5. The Corporation's mission statement should be formally approved by the shareholder provinces.	**ALC 96** - ALC's mission statement has been approved by its Board of Directors and will be reaffirmed at the next annual shareholders' meeting. **ALC July/97** - To have the mission statement reaffirmed at the next annual shareholders' meeting on June 16, 1997. **ALC Nov/97 Update** - The ALC Strategic Plan was approved October 6, 1997.

Recommendations for Consideration	Status of Action Taken or Planned
Accountability to the Legislature 6. Sufficient, appropriate and timely accountability information and reporting on ALC's plans and performance should be provided to the responsible Minister in each shareholder province, so such is available for tabling or deemed tabling in the respective Legislature.	**ALC 96** - ALC is considering enhancements to its annual report. ALC's annual report is widely distributed and is available to all on request. ALC will consider an even wider distribution. Tabling of reports in Legislatures is a shareholder decision. **ALC July/97** - The Public Relations department intends to develop a government relations program that will include the development of regular communication elements to keep shareholders informed of the operations of the Atlantic Lottery Corporation. The information gathered from the strategic planning team responsible for shareholder relations will be a source of ideas for developing the program. Additional disclosure discussed at the June 16, 1997 Board meeting. The Board agreed to the level of disclosure for the 1996-97 Annual Report. Disclosure for the 1997-98 Annual Report is to be considered at that time. **ALC Nov/97 Update** - The Public Relations department is in the process of identifying objectives and resource requirements for the government relations program. It will be submitted through the budget process, for consideration by the Board. ***NSGC 97*** *- Additional disclosure was provided for the fiscal 1997 financial statements. Also, distribution of the annual report was increased.* *ALC has improved information and reporting in 1997 and continues to evaluate further disclosure for 1998. Also, NSGC's annual and quarterly financial statements, which are tabled in the legislature, are more detailed than ALC's.*
Corporation's Annual Report 7. ALC's annual report distribution should be expanded, including tabling or deemed tabling in the Legislature on a timely basis.	**ALC 96** - ALC is considering enhancements to its annual report. ALC's annual report is widely distributed and is available to all on request. ALC will consider an even wider distribution. Tabling of reports in Legislatures is a shareholder decision. **ALC July/97** - The Public Relations department has already expanded its distribution list for the Annual Report to ensure the appropriate ministers and other government officials receive the report.

Recommendations for Consideration	Status of Action Taken or Planned
7. (Continued)	Additional disclosure discussed at the June 16, 1997 Board meeting. The Board agreed to the level of disclosure appropriate for the 1996-97 Annual Report. Disclosure for the 1997-98 Annual Report is to be considered at that time. ***NSGC 97*** *- NSGC's annual and quarterly financial statements, which are tabled in the legislature, are more detailed than ALC's.*
8. ALC's annual report should include sufficient and appropriate information on the performance of the Corporation, especially in relation to its defined plans, budget and goals. For example: - financial and other information on the Corporations's plans and performance against its strategic goals/objectives and its approved annual budget, with an appropriate emphasis on results compared to planned outcomes; - segregated and full-cost reporting of the results for the video lottery program, including information re: cash-in, credits won, credits played and cash-out. - increased information on the costs or expenditures of the Corporation (e.g., management compensation, travel expenses, major supply and service arrangements, external/consulting services, and/or other significant costs); and - appropriate per capita (i.e., per adult population) information and trends re: sales results and targets.	**ALC 96** - ALC is considering enhancements to its annual report. ALC's annual report is widely distributed and is available to all on request. ALC will consider an even wider distribution. Tabling of reports in Legislatures is a shareholder decision. **ALC July/97** - ALC is dealing with external auditors and others in considering enhancements to its annual report. The Finance department is dealing with external auditors and the Board in bringing forth both short-term fixes and more long-term planning required to deal with reporting issues that cannot be dealt with in the short term.
Board of Directors 9. In order to support an improved and modernized Board governance function, as part of a review of the inter-provincial agreements (which would encompass the Corporation's bylaws), the Board structure and complement should also be considered.	**ALC 96** - The Board believes the Board structure and complement are appropriately constituted. **ALC July/97** - None; unless and until management receives Board direction. Revised bylaws were approved by the Board in October 1992. ***NSGC 97*** *- NSGC has undertaken a full review of corporate governance issues related to ALC, including NSGC's role as a shareholder of ALC and ALC's role as agent for NSGC. This includes a review of all agreements, bylaws and relevant statutes and regulations.*

Recommendations for Consideration	Status of Action Taken or Planned
10. The Board should ensure that appropriate comprehensive standards governing Board, management, and staff behavior are adopted for ALC.	**ALC 96** - ALC has these in place and continues to enhance such standards in keeping with appropriate national corporate standards of ethics. **ALC July/97** - An outside ethics consultant has been engaged to provide services in the following areas: 1) document review 2) ethics code development 3) sniff test **ALC Nov/97 Update** - A Code of Ethics was approved by the Board October 6, 1997
11. The minutes of the Board meetings should provide an appropriate audit/management trail (i.e., re: the background and rationale for significant deliberations and decisions) and also provide an indication of the voting results for Board decisions (e.g., unanimous, approved - number of votes for, against and abstentions).	**ALC 96** - In order to ensure more comprehensive recording of minutes, a recording secretary now attends Board meetings. Board decisions are recorded by majority and only in instances where a Board member so requests is an individual vote identified. **ALC July/97** - Action has preceded the AG's report and recommendations as per ALC response. Also, the ALC Board has implemented "closed sessions" as a standard Board agenda item without attendance of management and the recording secretary.
12. The process for controlling and following up on the status of action taken or planned as a result of Board decisions or requests should be more formalized.	**ALC 96** - Board members are briefed on previous and outstanding business during two recurring agenda items: the President's report and matters arising from previous minutes. We will give consideration to a more formalized process. **ALC July/97** - As noted in Recommendation #11, a recording secretary now attends Board meetings. This should enhance controlling and following up on status of action taken or planned as a result of Board decisions or requests. A follow up report is also generated. Also, Internal Audit is investigating software solutions for tracking and monitoring of recommendations. If appropriate, the software solutions will be shared with the President's office/recording secretary. **ALC Nov/97 Update** - Several software solutions have been sourced and will be sampled and tested before committing to any one source.

Recommendations for Consideration	Status of Action Taken or Planned
Overall Management Control Framework 13. The preparation of current Corporate and other key divisional or program specific strategic plans, with appropriate input, involvement and approval by the Board and shareholder provinces, should be completed as soon as possible.	**ALC 96** - Corporate strategic planning is in process. Key divisional and program specific strategic plans have been conducted, others are currently in progress, and yet others will be revised/redone at the appropriate time. **ALC July/97** - Corporate strategic planning is currently underway. ALC has engaged the firm of Coopers & Lybrand to provide services for this planning. Board involvement is recommended. An update was handed out to the Board on June 9, 1997. The Strategic Plan will be further discussed with the Board at the August 25, 1997, meeting. **ALC Nov/97 Update** - The Corporate Strategic Plan was approved by the Board October 6, 1997.
14. ALC's internal and external reporting should include appropriate information on its plans and performance against the Corporation's approved strategic goals/objectives, using defined outcome measures or indicators.	**ALC 96** - Corporate strategic planning is in process. Key divisional and program specific strategic plans have been conducted, others are currently in progress, and yet others will be revised/redone at the appropriate time. **ALC July/97** - Refer to 13 and ALC Response under 15.
15. ALC should continue efforts to increase and enhance its use of performance indicators/targets at both the Corporate and the divisional levels, and to the extent possible, measurable indicators should be defined focusing on planned outcomes.	**ALC 96** -Corporate strategic planning is in process. Key divisional and program specific strategic plans have been conducted, others are currently in progress, and yet others will be revised/redone at the appropriate time. **ALC July/97** - Refer to 13 and above response.
16. ALC should move to a multi-year budget process, and continue efforts to enhance the contents and presentation of the supporting information in the Board's budget manual.	**ALC 96** - ALC has a multi-year strategic planning process in place; however, the Board prefers to approve budgets on an annual basis. **ALC July/97** - As noted in 13, 14, 15, ALC is currently undergoing strategic planning exercises with the assistance of Coopers & Lybrand. **ALC Nov/97 Update** - The Strategic Plan was approved by the Board October 6, 1997. ***NSGC 97*** - *Strategic planning is being conducted which will help to ensure, among other things, the adequacy of the information presented to the Board.* *The comprehensive budget process is under review at ALC. The process involves long term planning by the Board of Directors; translating this information into goals for management; and determining how these goals will be measured.*
17. ALC's financial statement disclosure of total divisional operating expenses should include depreciation expense.	**ALC 96** - This recommendation will be considered. **ALC July/97** - Recommendation has been implemented.

Recommendations for Consideration	Status of Action Taken or Planned
18. ALC’s internal/interim financial reporting and variance analysis should also provide a continuing link back to the original approved budget for a fiscal period.	**ALC 96** - This has been implemented. **ALC July/97** - Recommendation has been implemented.
19. ALC’s annual reporting (e.g., through its financial statements or otherwise) should provide a comparison to the original approved budget for the fiscal period.	**ALC 96** - This recommendation will be considered. **ALC July/97** - The Board did not include this in the 1996-1997 Annual Report, but it has been implemented for Board reporting and will be further considered for the 1997-1998 Annual Report.
20. As part of its review and approval of internal audit’s annual plans, the Board - through the audit committee - needs to consider whether, and ensure there are, sufficient and appropriate resources available, and that they are deployed in the areas that can be of greatest benefit to the overall level of control for the Corporation.	**ALC 96** - ALC has always placed emphasis on the internal audit function and will continue to do so. **ALC July/97** - Internal Audit is preparing formal annual plans and investigating our audit universe for more long-range planning. Internal Audit will be seeking audit requests (short and long term) from the Audit Committee and senior management. Impact on resources, to include the use of outside resources, will be brought forward to the Audit Committee for consideration. **ALC Nov/97 Update** - Internal Audit’s short term plans and staffing resources were reported to the Audit Committee meeting October 27, 1997.
Video Lottery Program 21. ALC should provide schedules segmenting the gross profit portion of the statement of operations by program type in its annual financial statements.	**ALC 96** - ALC will implement this recommendation in this year’s annual report. **ALC July/97** - Recommendation has been implemented.

Recommendations for Consideration	Status of Action Taken or Planned
22. ALC should be required to provide a detailed statement on the video lottery program reconciling the results of operations to the required payout specified in each shareholder province's regulations.	**ALC 96** - ALC will consider whether to implement this in the future; however, we are aware that most lottery jurisdictions in North America do not provide this level of detail in their annual reports. **ALC July/97** - The implications of this recommendation are being investigated. Including the following: 1) KPMG letter dated April 3, 1997 2) VLP outstanding issues - IT effort required to pursue the recommendation. LOG #26007: GAA is required to reconcile credits played/won to cash in/cash out. Current processes do not support this requirement. This log is a request for System Development to look at effort to modify processes to support this. IMPACT: A recent review by the NS Auditor General recommends that these values be reconciled and reported on ALC's financial statements. This cannot be done without system changes. STATUS: A meeting was held on April 14, 1997 where the issues around reconciliation of these values was discussed. After this discussion, Systems Development was tasked to size some potential changes to assist in this matter and the impacted user groups (GAA & Hotline) were asked to look at the impact on their current processes. A follow-up meeting was held on April 21, 1997 where the findings were discussed. It was determined at this meeting that more analysis around the potential solutions from Systems Development would be looked at further and also that we would determine if the number of exceptions that would require reconciliation would be too great to be handled using a manual reconciliation procedure. The results of these analysis are expected by the end of the week (Apr. 25). **ALC Nov/97 Update** - Work on the project continues with anticipated implementation within the fiscal year.

Recommendations for Consideration	Status of Action Taken or Planned
23. The methodology for allocating costs and profits to the gaming programs and to the shareholder provinces should be subject to a comprehensive review to ensure ALC's costs and profits are shared and reported on an appropriate and reasonable basis.	**ALC 96** - Shareholders have looked at this from time to time and will continue to do so. This will be again reviewed as part of the conduct of the economic benefit study. **ALC July/97** - An RFP has been issued (limited by Board of Directors to four accounting firms; only one response was received) for an economic benefit study to include a review of the profit allocation methodology. The RFP requires a final report by August 25, 1997. Profit distribution methodology based on Nova Scotia's proposal is being reviewed with board members. **ALC Nov/97 Update** - Economic Benefit Study has been received and reviewed by the Board. Additional information is being prepared. The Board and Shareholders are continuing to review profit distribution methodologies.
24. The commission rates paid should be assessed to determine if the current commissions deliver an appropriate return in line with the costs and risks associated with those components of ALC's operations.	**ALC 96** - Commission rates are established nationally by ILC or, in Atlantic Canada, by the shareholders. **ALC July/97** - None, except to respond to shareholder directives and/or announcements. ***NSGC 97*** - *Current agreement with the Nova Scotia Lounge and Beverage Room Association ends April 1, 1998 and will be reviewed by NSGC at that time.*
Information Technology (IT) 25. The management and control of ALC's information technology systems and resources should be subjected to additional and comprehensive audit coverage.	**ALC 96** - When the ALC Board approved the IT strategic plan, they also directed that an independent audit be conducted by an outside firm on IT subsequent to the implementation of the strategic plan. This will be done. Other audit coverages have either been done or are being considered. **ALC July/97** - As part of its planning, Internal Audit has identified the need for comprehensive audit coverage of IT systems and resources. A relatively new one person Internal Audit IT resource was created, more may be required. Internal Audit recommends, in <u>addition</u> to the Board directive noted under "ALC Response", an annual audit of IT conducted, in cooperation with Internal Audit, by an outside source. This is in keeping with the practices of other lottery jurisdictions. **ALC Nov/97 Update** - Internal Audit plans and staffing resources were reported to the Audit Committee at the October 27, 1997 meeting.

Recommendations for Consideration	Status of Action Taken or Planned
Procurement 26. ALC should prepare standard reports of its procurement activity in a manner consistent with the Atlantic Procurement Agreement, Section 9.	**ALC 96** - While ALC is not subject to the requirements of the Atlantic Procurement Agreement, the Board instructed ALC on March 7, 1994, to incorporate, wherever possible, the general intent of the Agreement into its procurement policies. **ALC July/97** - The Atlantic Lottery Corporation will prepare a quarterly report for the information of the Board of Directors in a manner consistent with the Atlantic Procurement Agreement, Section 9. **ALC Nov/97 Update** - Recommendation has been implemented.
27. ALC should continue to periodically evaluate its list of exceptions to standard procurement practices to ensure economic acquisition of goods and services. For example, given the current competition in the telecommunications market, ALC should consider tendering for those services.	**ALC 96** - ALC is currently doing this. **ALC July/97** - ALC is constantly evaluating its list of exceptions. Procurement maintains a short list of exceptions. Telecommunications is on this list. IT has stated, "We have begun to source Telecom Services competitively and will continue to do so in a controlled manner, in order to not adversely affect the integrity/reliability of mission critical services and to maintain the leverage of bulk purchasing."
28. ALC should formally document as part of its purchasing policy its practice of specifying initial contract terms and the renewal period. Further, formal documentation should be required of the contract review and evaluation process prior to the award of a contract extension.	**ALC 96** - The procedures were changed in 1993 and are documented in the new purchasing policies. Contract review and evaluations have been and continue to be documented. **ALC July/97** - To enhance the documentation, Purchasing is in the process of developing a template that will be used for contract reviews and evaluations. This template will be implemented by the end of July 1997. **ALC Nov/97 Update** - Recommendation has been implemented.

Recommendations for Consideration	Status of Action Taken or Planned
Allocations to Shareholders 29. ALC's reporting to its Board and external interested parties of the results of the VLP and its other gaming programs should be clearly segregated and on a more full-cost basis to the extent practical and appropriate. As a minimum, the results down to gross profit by program by shareholder province should be reported.	**ALC 96** - See 21, 23 **ALC July/97** - Finance is constructing the framework to provide for reporting of results separately for traditional and video lottery programs. This includes the allocation of employee and employee related expenses and an examination of all other operating expenses to determine which can be recorded directly to video lottery and which should be allocated and on what basis. **ALC Nov/97 Update** - An initial segregation of results has taken place effective October, 1997 separating Traditional and Video Lottery activity at a corporate level. The next phase of full cost reporting is to further segment these two categories into the four provinces. This will involve both expenses that are directly attributable to a single shareholder province and allocation of common operating expenses and other overheads. Although we are limited in our resources to accomplish this, we are confident it will take place before the end of this fiscal year. This will allow for a more full cost disclosure of programs by province in the 1997-98 annual report.
30. Where staff are directly involved in significant and continuing efforts related to regulatory or other activities associated with one or more but not all shareholder provinces, consideration should be given to allocating reasonable and appropriate costs to the specific shareholders concerned.	**ALC 96** - This will be considered **ALC July/97** - Refer to 23 and 29. An economic benefit study, including profit allocation methodology review, is to be conducted with a final report target date of August 25, 1997. Finance has taken steps to look at cost allocations. Resource implications will have to be considered in Finance and in other departments and divisions. **ALC Nov/97 Update** - see Recommendation 29

15.

QUEEN ELIZABETH II HEALTH SCIENCES CENTRE - REVIEW OF EXTERNAL AUDITOR'S MANAGEMENT LETTER

BACKGROUND

15.1 The financial statements of the Queen Elizabeth II Health Sciences Centre are audited by a public accounting firm. The Auditor General receives audited financial statements and copies of management letters issued by the Centre's auditors which include findings and recommendations to management.

15.2 We received a copy of a management letter from the Centre's auditors to the Centre's President and Chief Executive Officer dated July 29, 1997. The letter included certain comments which we deem to be significant enough to bring to the attention of the House of Assembly. In addition, certain less significant findings related to weaknesses in internal controls are reported in paragraph 17.7 of this Report, page 190.

RESULTS IN BRIEF

15.3 The following are the principal observations resulting from our review of the management letter issued by the Centre's external auditors.

- The Centre had an operating loss of $12.5 million and an accumulated operating deficiency of $21.9 million at the end of 1996-97. Management also anticipates operating losses of $11.9 million in 1997-98. The Centre is implementing a reengineering initiative which Centre management anticipates will generate total savings of $38 million by the year 1999-2000. The auditors have indicated that "*should savings levels not be obtained and deficits continue to escalate, then the provincial government will have to underwrite those deficits in order for the hospital to continue to meet its financial obligations and continue as a going concern.*"

- The Centre has recorded certain amounts as receivable from the Department of Health and Workers' Compensation Board which may not be entirely collectible. If these amounts are not collected, recognition of the uncollectibility will increase the Centre's forecasted deficit.

- The auditors found some instances where severance payments were made to employees under both the Compensation Assistance Program/Labour Adjustment Strategy and the Early Retirement Incentive Program. The Department of Health does not allow employees to benefit from both programs. To date, $335,000 of the related receivable from the Department of Health has been written off due partially to overpayments. The Centre's auditors recommend "*that the causes of the double payments be investigated and proper controls put in place to ensure that it does not continue to happen. The possibility of recovery should also be investigated.*"

- The capital costs of the renovation projects for the New Halifax Infirmary and the Victoria General Sites were 50% over budget. The Centre's auditors recommend *"that all future capital projects be carefully planned and budgeted by staff who are technically skilled and knowledgeable about the project. There should be strict budget controls throughout the entire project."*

Scope Of Review

15.4 We reviewed the management letter of the Centre's external auditors to the President and Chief Executive Officer dated July 29, 1997. We did not perform any additional verification of the audit findings and information included in that letter.

Principal Findings

15.5 The following comments are extracted from the July 29, 1997 letter from the Centre's auditors to the President and Chief Executive Officer.

Operations

The Financial statements reflect an operating loss of $12.5 million and an accumulated operating deficiency of $21.9 million at the end of the current year. The hospital administration had budgeted for an operating loss of $24 million, however, significant savings and expense reductions resulted in reducing anticipated losses for the current fiscal year.

The hospital has a bank indebtedness of $14.5 million as of March 31, 1997. Management anticipate operating losses of $11.9 million in the next fiscal year. In addition to operating losses, management have planned for capital projects of $24.9 million and investment in reengineering of $8.4 million which, when added to the operating losses, will require funding of $45.7 million. This results in a total cash requirement of $44.5 million in addition to the existing $14.5 million operating line currently in use, for a potential borrowings of $60 million next year to finance accumulated deficits.

The hospital is operating at $316,000,000 total expenditures for 1996/97 fiscal year. Excluding inflation, management forecast expenditures can be maintained at this level. Management have been required by government to reduce the annual cost of operations by reducing the revenue from Government.

As a response, the hospital has commenced a major reorganization of the way it does business by retaining consultants to advise management on a major reengineering of operations. The project is under way with savings expected to be realized commencing in the coming year. As at March 31, 1997, the hospital has invested $2.1 in the project and anticipate an additional investment of $8.4 in the current year. Targeted cost reductions over the next three years are $4.8 million in 1997/98, $22.4 million in 1998/99 and $10.5 million in 1999/00 for a combined savings of $37.7 million.

The actions by management and the level of funding support provided by the Province will impact on the potential savings identified by management. If the deficit is not fully funded or should management not implement change then the planned savings will be at risk.

Labour negotiations will commence this autumn with the union. These negotiations will have a significant impact on the financial position of the institution. Management have not provided for any significant salary adjustments arising from settlement with union employees in their business plan. Any settlement beyond the current collective agreement will result in non-budgeted losses for which the hospital has no source of revenue beyond the Province of Nova Scotia.

Should savings levels not be obtained and deficits continue to escalate, then the provincial government will have to underwrite those deficits in order for the hospital to continue to meet its financial obligations and continue as a going concern.

Capital Renovations

During the audit, we were requested to review the control processes in place as they relate to the capital renovation projects for the New Halifax Infirmary and the Victoria General Sites.

A brief summary of our conclusions arising from our audit are as follows:

The capital cost of the renovation project were overrun by 50%. This was due, in our opinion to:

1. A failure to budget the project properly including the omission of the project managers fees.

2. The project was not properly controlled by the administration of the hospital with the result that numerous charges were initiated by clinical managers during all phases of the renovations which resulted in substantial extras which were not subject to budget controls.

3. Failure by the project managers to control the projects within a predetermined budget.

We recommend that all future capital projects be carefully planned and budgeted by staff who are technically skilled and knowledgeable about the project. There should be strict budget controls throughout the entire project.

Accounts Receivable - Workers' Compensation Board

A receivable of $3.967 million from the Workers' Compensation Board continues to be carried on the accounts of the hospital as at March 31, 1997. This is a result of air quality problems at the old Camp Hill Hospital. This receivable is largely unchanged from last year, however management contends it remains collectible by virtue of no claims having ever been rejected in the appeal process. The appeal process is very slow and cannot be accelerated as the WCB process each claim through an extended appeal process, if necessary. During the current year, $19,000 in claims were approved and paid.

It has been, and continues to be the contention of management, should the WCB reject any individual claims, the provincial government will indemnify the hospital. There is no written commitment from the provincial government to support management's assumption.

We recommend hospital management pursue this item aggressively with both the provincial government and the WCB to come to a resolution. If the aggregate of claims cannot be resolved within a relatively short period of time, the hospital may have to recognize a loss on this account receivable and look to the Province of Nova Scotia to fund this additional loss.

Accounts Receivable - Department of Health

In last year's management letter, we identified a discrepancy between the Department of Health audit confirmation, and the hospital's financial statements. The nature of the discrepancy relates to environmental claims paid to employees during the time period of December 3, 1993 to March 31, 1994. The DOH could not acknowledge they owe this amount because they insist that no claim has been filed with them for this item.

As stated last year, if the hospital does not substantiate this claim, then the hospital will have additional deficit of up to $1.9 million which has not been budgeted. During the course of our audit, we determined that the administration have still not provided the necessary documentation.

We recommend that the required information to facilitate payment of this claim be compiled and forwarded to the Department of Health immediately. If this issue is not resolved within a reasonable time frame, then it should be written-off.

Included in the DOH net receivable is $2.30 million in environmental claims which date back to the 1993/94 and 1994/95 fiscal years. The DOH have confirmed these amounts in each of the last two years for audit purposes, but have not forwarded payment.

We recommend management request payment from DOH for this account receivable.

Included in the DOH net receivable is $3.28 related to the move into the new Halifax Infirmary. The DOH agreed in principle to fund the move expenses and have confirmed, for audit purposes, an amount owing of $1.7 million. Management have indicated that discussions have taken place with DOH on this issue and feel the receivable will be recovered in full. An agreed upon settlement amount has not been confirmed in writing.

We recommend management pursue collection of this account receivable immediately. If DOH do not make payment, then the $1.58 difference will represent an unbudgeted loss for which the hospital has no other source of funding.

The receivable from Department of Health for severance payments to former QEII employees is $5.401 million. This is made up of both Compensation Assistance Program/Labour Adjustment Strategy (CAP/LAS) and Early Retirement Incentive Program (ERIP) programs. The receivable is based on actual payments by the hospital to former employees, while the claims to DOH have been made by Human Resources.

Based on representations of management, severance payments were paid to some employees under both programs. DOH does not allow employees to benefit from both programs. There were also instances where payments were made above the maximum allowed. During the year, the hospital contracted a senior accountant to ensure all claims were submitted to the Department of Health. The amount of the loss to the QEII has not been determined. To date, $335,000 of the receivable has been written off due to overpayments and unrefundable miscellaneous costs.

We recommend that the causes of the double payments be investigated and proper controls put in place to ensure that it does not continue to happen. The possibility of recovery should also be investigated. We also recommend that reconciliation between the receivable and the approvals and rejections from DOH be done regularly.

15

CONCLUDING REMARKS

15.6 The external auditors of the Queen Elizabeth II Health Sciences Centre have expressed concerns about the financial position of the Centre in relation to the accumulated deficit and anticipated future deficits. The Centre plans to recover these deficits through future cost savings. If the planned savings do not occur, then the Province and Centre will have to deal with the question of how to finance large accumulated deficits. The situation is serious enough to warrant careful monitoring by the Department of Health and the government.

RESPONSE OF DEPARTMENT OF HEALTH AND QEII HEALTH SCIENCES CENTRE

Operations

The Department of Health and the QEII Health Sciences Centre entered into a multi year business plan in March 1996. This plan anticipated the QEII operating at a deficit position in the early years of the plan to allow them to implement efficiencies over several years. These efficiencies would allow the QEII to repay this deficit and operate with a balanced budget.

At the end of the first year of the plan, the QEII was on target with respect to its operating results and had identified many areas where efficiencies to reduce operating costs could be implemented.

During 1997/98, the QEII and the Department of Health have continued to meet regularly to review the financial position of the QEII. Where deviations from the original business plan have occurred, the Department has provided additional funding to the QEII to compensate for this.

With any multi year plan it is expected that the actual funding levels will be reviewed and adjusted as the plan unfolds. This is the strategy being used by the QEII and the Department of Health in managing the financial position of the QEII.

Capital Renovations

The following changes have been implemented to address concerns raised through the audit:

Budget

- *Budgets are prepared by the Director, Engineering Services and the managers of Facility Planning and Renovations in consultation with program planning staff, other departmental staff and with the input of external architectural expertise. These budgets are reviewed by Financial and Corporate Services.*
- *Annual renovations' budgets must be approved by the Vice President, Diagnostic and Therapeutic Services and by the Vice President, Financial and Corporate Services.*
- *Final renovation budgets are approved by the Finance and Audit Committee of the Board of Directors.*
- *Budgetary performance rests with the Vice President, Diagnostic and Therapeutic Services through the Director, Engineering Services and the managers of Facility Planning and Renovations.*
- *Contingencies have been established to fund change orders and other project uncertainties. Project managers are expected to manage the change process to the level of established contingency.*

Tendering

- *Project work must be tendered based upon specifications developed by in-house staff with assistance of external architects.*

Infrastructure/Reporting

- *A detailed project listing, complete with actual, budget, projected and percentage complete information is sent to the Audit and Finance Committee each month. Engineering Services provides all projected and percentage completed information.*
- *Project costing records kept by Engineering Services are reconciled to Financial and Corporate Services records on a regular basis.*

Accounts Receivable - Workers Compensation Board and Department of Health

With respect to accounts receivable from Workers Compensation Board and the Department of Health, the QEII and the Department continue to work closely to resolve these issues.

The Occupational Health staff at QEII and the Director of Human Resources at Department of Health have been meeting regularly to develop a strategy for addressing the issues of WCB management and environmental health issues.

The Department of Health has funded the QEII for both the outstanding environmental illness claims and the costs of the move to the New Infirmary.

With respect to the CAP/LAS and ERIP programs, the QEII has reviewed this process and have made modifications to the process to ensure that payments under both plans no longer occur. In addition, the QEII has begun to reconcile outstanding claims monthly.

16.

RESOURCE RECOVERY FUND BOARD INCORPORATED

BACKGROUND

16.1 The Resource Recovery Fund was established by the Province in 1990 to provide financial support for waste management practices and to encourage recycling and protection of the environment. In 1995-96 the Province developed the Solid Waste-Resource Management strategy which committed the Province to achieving 50% waste diversion by the year 2000. On February 6, 1996 the Province repealed regulations under several acts and created Solid Waste-Resource Management Regulations under Section 102 of the Environment Act. The strategy called for the administration of the Resource Recovery Fund to be transferred to a private sector, not-for-profit organization which would be responsible for managing a substantial portion of the Solid Waste-Resource Management Regulations.

16.2 The Resource Recovery Fund Board Incorporated (RRFB) was established on January 5, 1996 under the Companies Act of Nova Scotia as a not-for-profit corporation. On February 6, 1996 the RRFB entered into a five-year agreement with the Province to administer the Resource Recovery Fund and to achieve the following five objectives.

- Develop and implement industry stewardship programs.
- Fund municipal or regional diversion programs.
- Develop and operate a deposit-refund system for beverage containers.
- Develop education and awareness of waste-resource reduction, reuse, recycling and composting.
- Promote the development of value-added manufacturing in the Province.

16.3 According to its Articles of Association, the RRFB may have between seven and fifteen members on its Board of Directors. Regulations empower the Minister of Environment to appoint three members, one of whom is the Chair, and the RRFB appoints one director who is a nominee from the Union of Nova Scotia Municipalities. The remainder are appointed by the Board, and at the time of our audit the RRFB had nine directors. The RRFB is accountable to the Minister of Environment and must follow an annual action plan approved by the Minister.

16.4 For the year ended March 31, 1997 the RRFB had total revenues of $17.1 million, expenditures of $14.4 million and a surplus of $2.7 million. The surplus was used, in part, to fund external education and awareness initiatives ($334,361), regional waste coordinators ($137,500), and solid waste diversion in municipalities ($1,149,202).

16.5 The ultimate goal of the RRFB is to help the Province achieve 50% solid waste diversion by the year 2000. According to Department of Environment statistics, 26.6% diversion had been achieved by March 31, 1997. The Province is divided into seven regions for purposes of the Solid Waste-Resource Management Strategy, and progress to the diversion target was estimated as 55.8% in the Halifax region, but only 2.0% in the Cape Breton region. The other 5 regions were in the 5.4% to 13.7% waste diversion range.

RESULTS IN BRIEF

16.6 The following are the principal observations from this audit.

- Although the RRFB was incorporated as a private, not-for-profit company, it is administering government programs and assets, and is responsible to government for its activities. Accountability for public funds would be better served by formally presenting the RRFB's annual report and business plan to the House of Assembly.

- The RRFB remitted $250,000 in Goods and Services Tax, net of rebates, in the year ended March 31, 1997. With the implementation of Harmonized Sales Tax, the RRFB is now paying sales tax to the Province as well. It is unclear whether a different, tax-exempt form of organization would have created other difficulties in the accomplishment of the RRFB's goals.

- The responsibilities and accountability of the RRFB are well defined in regulations and a formal agreement, and we observed compliance by RRFB with most significant requirements. However, we noted an absence of minutes for certain meetings of the Board of Directors and failure to include a summary action plan and reporting on compliance with the code of conduct in the annual report.

- The RRFB's annual report is well organized, understandable and adequately accounts for its activities and performance. We have recommended making the report more complete by addressing all materials banned from landfills and incinerators.

- Planning at the RRFB is organized, strategic, timely and addresses an appropriate future period. However, there is little evidence of formal strategic planning during the first year of the RRFB's operation.

- Roles, responsibilities and powers for enforcing compliance with the rules of the beverage container deposit and tire recycling programs have not been established. To date, there has been insufficient compliance auditing of beverage distributors and tire retailers.

- Several recommendations were made to improve internal control. These included more timely financial reporting, improved segregation of duties and approval of journal entries.

- The RRFB used processes to ensure goods and services were acquired at competitive prices. However, we were not able to conclude whether value-for-money was achieved from the RRFB's contracting with the Clean Nova Scotia Foundation.

- The minutes of RRFB Board of Director meetings describe situations where it appears certain directors were not in compliance with the RRFB's code of conduct.

AUDIT SCOPE

16.7 In September 1997 we commenced a broad scope audit of the RRFB in accordance with the provisions of the Auditor General Act. The RRFB was incorporated as a private, not-for-profit corporation. However, we have established that the RRFB administers public funds and has a direct responsibility to the Crown through the Minister of Environment. Sections 2 and 8 of the Auditor General Act address these issues and give the Auditor General an audit mandate in this situation.

16.8 Our audit objectives were to examine and assess:

- compliance with key provisions of the regulations to Section 102 of the Environment Act and with the February 1996 agreement with the Province of Nova Scotia;
- the accountability structure and reporting practices;
- strategic and operational planning practices;
- internal control over revenues and expenditures;
- controls within the computer environment and individual computer applications; and
- the policies and practices used to ensure due regard for economy and efficiency in the RRFB's procurement activities.

16.9 The following general criteria were used in our audit.

- The RRFB should comply with all requirements of relevant legislation, regulations and contractual agreements. Summary information on compliance should be reported annually to the Board of Directors and the Minister.
- Accountability and responsibilities should be formally defined and accountability reporting should be accurate and timely. Reporting should address performance relative to the RRFB goals and priorities, and should be supported by a system of performance measurement.
- Strategic and operational planning should be performed on a regular basis and be consistent with the RRFB's mandate. Goals should be outcome-oriented and measurable, where possible, and goals and other plans should be communicated to all staff.
- There should be an appropriate combination of Board of Directors, management, process and information system controls to ensure that all revenues are received and funds are only expended for authorized purposes.
- Procurement practices should ensure goods and services of an appropriate quality are acquired at the lowest possible cost, and only goods and services relevant to mandated operations are acquired.

16.10 Our audit objectives and criteria were reviewed with management at the beginning of the assignment. Our audit involved interviewing staff, performing detailed transaction testing, as well as examining reports, correspondence, agreements, minutes and other relevant documents.

PRINCIPAL FINDINGS

Organization, Accountability and Compliance with Authorities

16.11 On February 6, 1996 the RRFB entered into a five-year agreement with the Province to administer the Resource Recovery Fund and to achieve five goals noted in Section 4 of the Solid Waste-Resource Management Regulations. The RRFB is subject to the requirements of this agreement and these regulations, as well as those contained in its Articles of Association under the

Companies Act of Nova Scotia. We examined issues relating to the RRFB's organizational structure, accountability and compliance with authorities.

16.12 *Organizational structure* - The RRFB was incorporated on January 5, 1996 under the Companies Act of Nova Scotia as a not-for-profit entity. It is management's understanding that the RRFB was intended not to be an agency of the Provincial government and was to have the autonomy to direct its own operations. However, as noted above, the RRFB meets the definition of "agency of government" under the Auditor General Act. Furthermore, it meets the definition of "department" in accordance with the Provincial Finance Act, as it applies criteria almost identical to those described in the Auditor General Act. Both Acts consider an organization to be a government entity if *"... all the members of the board of management or board of directors of which, ... (i) for the proper discharge of their duties are, directly or indirectly, responsible to the Crown."* In our view, the requirement of RRFB directors to administer government-owned funds in accordance with regulations, and to follow government-approved action plans and to account to the Minister of Environment for their performance, indicates at least an indirect, if not fully direct, responsibility to the Crown.

16.13 This appears to be a unique organizational structure in Nova Scotia for the administration of government programs. Management of RRFB indicated that one of the reasons for this structure was to avoid suggestions that the recycling programs are just another means of raising revenue for the general operations of the government. The creation of an arm's-length entity to operate the programs would avoid such a perception, and would ensure all fees collected are channelled into environmental programs.

16.14 Senior officials at the Department of Environment have told us that a major reason for this unique structure was to create an agency that, because it was at arm's-length from government, would be more successful in negotiating environmental stewardship agreements with industry. The government wished to have industry participate voluntarily in stewardship programs and to avoid the use of regulatory measures. At the same time, there had to be strict accountability to the government because public funds were at stake.

16.15 We wish to note two issues relating to the organizational structure.

- *Reporting* - As noted above, the government has imposed strict accountability requirements on the RRFB by way of regulations. The regulations require reporting by the RRFB to the Minister of Environment, and that any such reports received by the Minister be considered public documents. In our opinion, these requirements serve the needs of the government and public, but do not address the information needs of the group ultimately responsible for the stewardship of public funds - the House of Assembly. We recommend that there be a formal requirement for the timely tabling of RRFB business plans and annual reports in the House of Assembly.

- *Sales tax* - The majority of RRFB's revenue is from a beverage container deposit program implemented on April 1, 1996. In 1996-97 Goods and Services Tax (GST) was paid to the Federal government by RRFB at a rate of 7% on all beverage container deposits received. This amounted to approximately $250,000, net of GST rebates. The Harmonized Sales Tax (HST) was implemented April 1, 1997 and subjected the deposit program to an additional 8% tax, representing the Province's portion. RRFB management estimate that, due to the introduction of HST, an additional $430,000 will be paid in tax in 1997-98. This will further reduce funds available for recycling programs and sharing with municipal governments. RRFB management has met with Nova Scotia Department of Finance officials to attempt to have the Provincial share of HST refunded, and they plan to continue to pursue the issue in 1998.

The crux of this issue is whether or not GST or HST would have been levied against beverage container deposits if the program was organized differently. For example, if the program was operated as a division of the Department of Environment, sales tax would likely not have been applicable. If the RRFB had been set up as a crown corporation, the issue would have been less clear. We cannot comment on the propriety of sales tax application and refunding, as we have no expertise in this area and it was not a focus of our audit. However, sales tax is a real cost to the government and public of Nova Scotia in the delivery of the beverage container deposit program. It is unclear whether the benefits of the organizational structure outweigh these additional costs.

16.16 In discussing these issues with management, we learned they were unaware that Provincial legislation suggests that the RRFB is an agency of government. They expressed concern about whether or not the RRFB must comply with government policies, such as those pertaining to procurement, wage-restraint and access to information. We recommend that RRFB management and government officials meet to clarify the RRFB's organizational structure and relationship to government.

16.17 *Accountability* - The accountabilities of the RRFB are defined in the regulations, the agreement with the Province and its incorporating Articles. The RRFB is ultimately accountable to the Minister of Environment. The agreement with the Province requires the RRFB to present an annual action plan to the Minister, and the plan must be followed after receiving approval from the Minister. The agreement also requires the RRFB to present to the Minister an annual report and audited financial statements.

16.18 We found that all significant accountabilities had been fulfilled by the RRFB. During 1997, the RRFB held meetings with the Minister and his staff. A Department of Environment official is a director of the RRFB and he attended Board of Directors and RRFB committee meetings. In April 1997 the RRFB presented its 1997-98 action plan to the Minister. In June 1997 the RRFB held an annual general meeting which was attended by the Minister and audited financial statements and an annual report were presented.

16.19 As part of our audit, we examined the RRFB's annual report to assess its value as an accountability document. In general, we found the report to be well organized, understandable and goal-oriented. We believe the reporting of performance could be more complete with respect to banned materials. The Minister designated 13 materials to be banned from landfills and incinerators, with 7 of them to be effective on or before April 1, 1997. The RRFB annual report only discusses one of these designated materials

16.20 *Compliance with authorities* - We reviewed the requirements imposed on the RRFB under the regulations, agreement and Articles of Association. Except for the instances noted below, all significant provisions and clauses were complied with.

16.21 We observed that the RRFB was not in full compliance with two clauses of its Articles of Association. Clause 78 discusses corporate minutes and requires that minutes be kept of meetings of directors. We found that minutes of four conference calls in the fall of 1996 (constituting formal meetings of the Board) were not entered in the minute books. Copies were eventually obtained during our audit in the fall of 1997 by petitioning individual directors. Clause 78 also requires that minutes be kept for meetings of committees of the Board, but no committee minutes were available during our audit. When we met with management to discuss the results of our audit, they indicated that minutes are now being maintained for all meetings of the Board and its committees.

16.22 We also found that the RRFB was not complying with section 11.03 of the agreement with the Province. Section 11.03(b) requires that the RRFB's Annual Report include a summary of its action plan and specific objectives. The 1997 Annual Report did not contain a summary of the action plan because one did not exist for 1996-97. An action plan was created for 1997-98, and management intends to include a summary of it in the 1998 Annual Report. Section 11.03(c) requires that the annual report include a report on the compliance and/or non-compliance of RRFB Board members with its code of conduct. The 1997 Annual Report did not address this matter.

16.23 In paragraph 16.65 below, we describe possible conflicts of interest on the Board of Directors.

Planning

16.24 The RRFB was created in January 1996. It operated for most of 1996 with very few staff. The Board of Directors was significantly involved in the day-to-day activities of the entity. However, no business plan or action plan was prepared to guide these activities. Accordingly, there is little evidence of formal strategic planning in the first year of the RRFB's operation.

16.25 The current management team was put in place during the summer and fall of 1996. In January 1997 management met with Department of Environment officials to determine the contents of the action plan required by RRFB's agreement with the government. Subsequently, RRFB staff prepared a financial budget and action plan for the 1997-98 year. In March 1997 the Board of Directors reviewed and approved the two items, and the plan was presented to the Minister in April 1997.

16.26 The action plan describes the RRFB's corporate mission and concentrates on the five goals listed in the agreement with the Province. Objectives have been set to promote progress toward the five goals. As well, the annual budget and five-year financial projections contained in the plan also focus on the prescribed goals. The plan reviews the achievements of 1996-97 and sets targets for 1997-98. There was participation by most RRFB staff in the preparation of the action plan and budget.

16.27 In our view, whereas formal planning was absent at the RRFB during its first year of operation, planning is now organized, strategic, timely and addresses an appropriate future period.

Internal Control

16.28 The RRFB is responsible for administering the beverage container deposit program. As well, it is responsible for other programs such as the recycling of used passenger and light truck tires. The beverage deposit program was implemented on April 1, 1996 and generated revenues of approximately $16.6 million and incurred expenses of $12.5 million in 1996-97. The 1997-98 budget forecasts revenues of $17.3 million and expenses of $13.9 million. Retailers of passenger and light truck tires were required to pay a recycling fee effective January 1, 1997. The tire recycling program generated approximately $290,000 revenue and incurred $166,000 of expenses in 1996-97. In 1997-98 the tire recycling program is expected to result in $2.3 million of revenue and $2.6 million of expenses.

16.29 Accounting services were provided by an accounting firm until April 1997, when responsibility for all accounting functions was assumed by RRFB staff. Accounting and other reports are prepared on a monthly basis for internal management review. Each quarter, various accounting and information reports are prepared for the Board of Directors.

16.30 The financial statements of the RRFB are examined by external auditors on an annual basis. The 1997 auditor's management letter identified a number of internal control weaknesses, including the fact that certain basic accounting procedures were not being performed. The external auditors returned in November 1997 to review the RRFB's progress in addressing their recommendations. In a letter to management, the auditors indicated they were pleased with the progress made.

16.31 We examined the systems used by the RRFB to ensure management and the Board of Directors receive appropriate, accurate and timely information necessary for monitoring operations and making decisions. As well, we reviewed systems used to control the processing of revenues and expenditures. Our findings are reported below.

16.32 *Compliance enforcement* - The RRFB collects beverage deposits from approximately 70 product distributors and collects tire fees from approximately 800 tire retailers. The RRFB was late in implementing procedures to verify sales information reported by distributors and retailers and, at the time of our audit, was not fully assured that all remittances received to date were complete and accurate. The beverage deposit program began in April 1996, but a search for a compliance auditor was not started until May 1997, 13 months after the beginning of the beverage container program. It took until October 1997 to find and hire a person suitable for the job. Compliance auditing of beverage distributors and tire retailers is a critical component of the RRFB's control systems, and we believe it should have been instituted closer to the beginning of the recycling programs.

16.33 Furthermore, payments to the RRFB are not always made on a timely basis and accompanied by the type of information the RRFB requires. RRFB staff follow up to ensure monthly remittances are received from all distributors and retailers. However, the RRFB cannot levy interest or penalties if the payments are not received on a timely basis or if the remittance information is not filed in the format required by the RRFB. This limits the authority of the RRFB to enforce compliance with the beverage container and tire recycling programs.

16.34 It appears that the primary cause of these problems is a lack of clarity in legislation and regulations as to responsibility for compliance enforcement activities. The Environment Act gives the Department of Environment the power to investigate and levy fines in certain situations. There is no such power provided to the RRFB. RRFB management have discussed the matter with Department officials, but there is no consensus yet. Management explored the possibility of contracting with the Provincial Tax Commission to perform audit services, but found the cost to be prohibitive. Because the lack of compliance enforcement is a serious control weakness for the RRFB, management proceeded with the hiring of a compliance auditor before the issue of responsibility and authority was rectified. We fully agree that compliance enforcement is important to the proper control of the RRFB, and we urge that the respective roles, duties and powers of RRFB and Department of Environment staff in this area be settled as soon as possible.

16.35 *Policies and system documentation* - The RRFB makes extensive use of computerized information systems, including electronic billing and payment of suppliers who are involved with the beverage container and tire programs. Computer operations are documented in a comprehensive system manual and the RRFB has begun to prepare a manual which documents manual processes and other policies. Examples of policies which still need to be developed include procedures for granting credit and collection of overdue accounts receivable.

16.36 *Financial reporting* - Financial statements are prepared monthly and distributed to senior management, and are presented at quarterly meetings of the Board of Directors. We observed that financial statements could be prepared on a more timely basis. In our opinion, monthly financial statements should be completed within two or three weeks after the end of the month. During our audit, the August 1997 financial statements were not available until mid-October. The Board received June quarterly financial statements at their September meeting. We believe financial information must be timely to be relevant and useful. Management has indicated to us that they have set a monthly reporting target of 20 days, and that they are currently meeting that goal.

16.37 In June 1997 the external auditor noted that there were several deficiencies in the recording of RRFB's accounts. We understand that all recommendations addressed at making the monthly financial statements more accurate have been implemented.

16.38 *Revenue processing* - It is important that adequate controls be in place to ensure all revenues due are received, accurately processed and recorded. The RRFB had in excess of $20 million in receipts in 1996-97. We reviewed the system to process revenues and have the following observations.

16.39 The RRFB uses a manual system to record the sale of recovered materials such as aluminum, cardboard and glass. The 1996-97 sales of these materials were in excess of $2 million. Currently it would be possible for materials to be sold and the sale not recorded in the accounts. The only control is a review of recorded revenues by the Controller. If the sale function was computerized, the RRFB would be able to automatically generate and record sale and accounts receivable transactions and also track recovered materials from the time they are shipped from the Enviro-Depots to the time they are sent to the final purchaser. The RRFB is exploring the feasibility of expanding computer systems to incorporate this function.

16.40 All beverage distributors and tire retailers are required to make monthly remittances to the RRFB, and in 1996-97 approximately $18 million were received in the mail from these sources. We reviewed staff responsibilities relating to cash receipts and found the need for better segregation of incompatible accounting duties. The staff member responsible for making bank deposits is also responsible for recording receipts, following up late payments, making adjustments to accounts receivable and preparing bank reconciliations. Proper segregation of duties requires the responsibility for handling funds to be separate from accounting duties so that errors and misappropriations cannot occur and remain undetected.

16.41 We observed that not all remittances are recorded in the mail log book. Internal control would be strengthened if all receipts were recorded in log books and totals were agreed to bank deposits by a person who is not responsible for handling cash receipts.

16.42 We also observed that adequate documentation was not prepared for journal entries which adjust accounts receivable. Also, the journal entries were not reviewed or approved by a second person. Management have indicated that all journal entries are now fully supported and reviewed.

16.43 *Expenditure processing* - It is important that adequate controls be in place to ensure all expenditures are accurately processed and recorded. Controls should also ensure that payments are made only after goods and services have been received and that correct prices are paid.

16.44 A computerized system is used to process payments to Enviro-Depots, local trucking companies and Regional Processing Centres (RPC's). In 1996-97 approximately $12.6 million was paid by electronic funds transfer to these entities. A series of edit checks have been built into the computer system to ensure the accuracy and completeness of these cash transactions. Enviro-Depots are paid based on the number of beverage containers shipped to RPC's. To test the accuracy of payments made to depots, bags of recyclables are recounted on a test basis. This procedure also allows the RRFB to determine if the depots are submitting only authorized containers for recycling. RPC's are paid based on the number of bags of material received from the depots and processed. In the following paragraphs we describe areas where control could be improved.

16.45 In 1996-97 the five RPC's were paid approximately $893,000 to process recyclable materials and to prepare them for further shipping. The RRFB had no written contracts with the RPC's during that period, nor for the subsequent six months. However, in the fall of 1997 management were able to finalize contracts with four of the five RPC's. We have recommended that the contract with the remaining RPC be executed as soon as possible.

16.46 The cost of the tire recycling program is budgeted to be $2.6 million in 1997-98. A tire recycling company is paid $1.25 for each used tire collected. The company submits an electronic monthly claim with supporting documentation for tires collected, but the RRFB does not agree or test the claim's details to its supporting documentation.

Computer Environment and Applications

16.47 Information systems are comprised of two major applications - a commercial accounting package and a custom-designed product control system. The custom application software receives data from suppliers, performs various edit tests on data received and calculates the payments due to the suppliers. The information is transferred to the accounting system and an electronic funds transfer is subsequently made by the product control system. The custom application also produces various management reports.

16.48 We examined various aspects of the computer control systems including the general computer environment, disaster recovery planning, program change controls, logical access controls and application processing controls. Generally, we found the controls in these areas were good. However, we noted certain areas where improvements should be considered.

16.49 *Disaster recovery planning* - Disaster recovery planning is the process of identifying procedures and guidelines to be used to recover from a loss of computer processing capacity. Contingency planning is the process that focuses on how an entity will maintain operations while the disaster recovery plan is being put into effect. Both plans are essential to allow for uninterrupted operations in the event of a disaster such as a flood or fire.

16.50 A disaster recovery and contingency plan has been prepared by RRFB. We have identified the need for more training of staff with respect to disaster recovery procedures.

16.51 *Logical access controls* - In information processing environments, logical access or password controls provide the primary means to restrict access to information systems and their related processes and functions. The purpose of such controls is to provide assurance that all access to information systems is authorized and in accordance with established policies and procedures. A well controlled computer application will restrict each user to the specific functions necessary to perform assigned responsibilities and tasks.

16.52 The controls in RRFB's accounting systems are adequate in this regard, though staff should be required to change their passwords on a regular basis. Also, the product control system was designed and implemented with a security function that only restricted overall access to the system. This weakness enables staff who have access to the system to have complete and unrestricted access to all system processes or functions. As such, it is more difficult for the RRFB to ensure only authorized persons use the computer system and that only appropriate uses are made of the system. We noted that the RRFB's external auditor recommended improvements in this area, and we understand that the designers of the product control system have recently been contracted to enhance the system's security functions.

Procurement

16.53 The RRFB was established in January 1996 and was required to develop a comprehensive beverage container deposit-refund program by April 1, 1996. Due to the tight deadline, the engagement of collection depots, transport companies and regional processing centres was not publicly tendered. For the most part, many existing bottle collection depots became Enviro-Depots, and a common rate was set for paying them. The RRFB held information sessions around the Province and asked that interested parties submit proposals for collection, transportation and processing services. The proposals were reviewed by staff, and in most cases, the lowest cost proposal was chosen.

16.54 We noted several instances where the selection of other services was by public tender or request for proposals. Based on our review of the procurement practices of the RRFB, we concluded that, in most cases, due regard was given to efficiency and economy. We describe below how due regard was given to economy and efficiency with respect to the setting of deposits and fees. However, we also describe dealings with Clean Nova Scotia Foundation where it is unclear to us whether value-for-money was achieved. We follow with a description of potential conflicts of interest on the Board of Directors concerning contracts with Clean Nova Scotia Foundation.

16.55 *Deposits and other fees* - In the development of the various recycling programs, rates were set for beverage container deposits, Enviro-Depot handling fees, tire recycling fees and payments to Regional Processing Centres (RPC's). As described below, it appears that adequate regard was given to economy and efficiency in the setting of the various rates.

16.56 The 10 cent beverage deposit was based, in part, on a deposit system that was already operating in another maritime province, and on the studies that supported that program. As part of the rate structure adopted, Enviro-Depots are paid a 2.5 cent fee for each beverage container handled. Analysis has led RRFB management to believe a depot can operate economically, as a stand-alone business, within this fee structure as long as the population base served remains above 25,000.

16.57 The RRFB implemented a recycling program for vehicle tires on January 1, 1997. The RRFB hired a consultant to review over 50 business proposals and to recommend a company to collect and process Nova Scotia's used tires. The consultant reviewed the proposals and chose two for in-depth analysis. The in-depth analysis compared and evaluated the two proposals against 13 criteria, including the amount of the tire recycling fee. The RRFB contracted with the company recommended by the consultant. We reviewed the consultant's recommendations and noted that the successful company proposed a lower fee, committed to having finished goods produced in Nova Scotia, and that no government assistance was to be provided to the company. We also observed that the negotiated tire fee appears consistent with the fee implemented or proposed in six other provinces.

16.58 The RRFB engaged five Regional Processing Centres (RPC's) in March 1996 based on proposals submitted to the RRFB at the outset of the beverage container deposit program. In some cases, the proposed fee was negotiated downward. The current group of RPC's are paid a fee for each bag of material processed, but fees range from $5.20 per bag to $7.50 per bag depending on the RPC. We have recommended that the RRFB conduct Province-wide competitions for the provision of processing services as contracts with RPC's expire.

16.59 *Clean Nova Scotia Foundation* - For the year ended March 31, 1997 the RRFB entered into four contracts with Clean Nova Scotia Foundation (CNSF). The contracts were for various public relations, awareness and education initiatives. None of the contracts were subject to a tender or a request for proposal process.

16.60 On March 29, 1996 based on a proposal from CNSF, the RRFB Board of Directors approved a three-month contract for $25,250 subject to receiving CNSF financial statements and monthly status reports. There is no record that the statements were ever received. During a July 1996 Directors' meeting it was noted that the required monthly progress reports had not been received, though in August 1996 a final report was provided.

16.61 In August 1996 the RRFB entered into a five-month contract with CNSF for $75,850 to set up a Waste Reduction Centre. The contract required monthly progress reports but only one report was received by the RRFB.

16.62 On October 17, 1996 the RRFB approved a five-month $133,398 contract with CNSF for education and awareness initiatives. The contract period was from August 1 to December 31, 1996, but we noted that CNSF was estimated to have spent between $90,000 and $100,000 on the initiatives before the contract was signed. The Chairman of RRFB wrote to CNSF on October 15, 1996 noting that he was surprised to learn that money was spent without a binding contract. The letter also noted that some of the work done by the CNSF was not in accordance with RRFB standards. The contract required monthly progress reports, but no reports were provided to RRFB.

16.63 On December 20, 1996 the RRFB approved a $400,000 contract which required quarterly performance reports. The contract is for the provision of services described in a November 29, 1996 proposal for operation of a Waste Reduction Centre for the RRFB. To date, reports are being received by RRFB, but it is not easy to determine from the reports whether or not all contracted services are being provided. Also, no information is provided in these reports or was provided before the contract was signed to indicate the cost to CNSF of performing these services.

16.64 We cannot determine whether or not value-for-money has been received from the CNSF contracts because:

- the services provided by CNSF were not subject to a tender or request for proposal process to ensure the cost of the services is competitive;
- the RRFB was never privy to CNSF's cost of providing the services;
- of 13 status reports required for three of the contracts, only two reports were received by RRFB; and
- certain directors had a conflict of interest, and the minutes of the Board indicate that some of these directors voted on matters related to CNSF on two occasions, as discussed below.

16.65 *Conflict of interest* - Section 53 of the RRFB Articles of Association notes that directors should declare any relevant interests and should refrain from voting in respect of a contract or other arrangement that conflicts with an interest they possess. The agreement with the Province also requires that the RRFB adopt a code of conduct to prevent any real or perceived conflict of interest and that the code shall be no less stringent than the rules under the Canada Business Corporations Act. We observed that the RRFB has a code of conduct consistent with the Act.

16.66 However, we reviewed minutes of Board of Directors' meetings and noted instances where an appearance of conflict of interest was given by the minutes. Although the minutes during this period were noted as approved by the Board in subsequent minutes, they were not signed by Board officials to indicate this approval.

16.67 During the March 13, 1996 Board of Directors' meeting, one director suggested that it was inappropriate and represented a conflict of interest for certain board members (who were also members of the Clean Nova Scotia Foundation) to involve themselves in discussion of a proposed contract between the RRFB and the CNSF. The Chair ruled that the CNSF members could participate in discussions, but should refrain from voting on issues relating to CNSF. However, we noted the following:

- During the July 26, 1996 meeting of Directors, approval was given to a five-month $210,000 contract with CNSF. Although current members of CNSF were present at the meeting, the minutes do not indicate any abstentions due to conflict of interest.
- During a October 17, 1996 Directors' meeting to discuss a five-month $133,398 contract for the CNSF to provide education and awareness services to the RRFB, eight directors participated and a director who had previously been identified as having a potential conflict was not named in the minutes as abstaining from voting.

CONCLUDING REMARKS

16.68 The RRFB is about two years old at the time of the writing of this Report, but the current management team have been on staff for a little over one-half of this period. We observed good attention to the need for regular and timely strategic planning, as well as a recognition of the importance of accounting for performance and achievement of goals.

16.69 The RRFB uses sophisticated technology to account for and control its operations, and we have found the systems to be well controlled. However, we believe more attention could be given to other areas of control, such as internal reporting, segregation of duties and establishing the roles and responsibility for compliance enforcement. As well, we recommend that attention be given to ensuring fair value is achieved in contracts for services with Clean Nova Scotia Foundation.

RESOURCE RECOVERY FUND BOARD INC.'S RESPONSE

We would like to thank the Auditor General's office for their comprehensive audit of the policies, practices and procedures of the Resource Recovery Fund Board Inc. (RRFB). Since signing an agreement with the Province in February 1996, RRFB staff have worked diligently to develop policies, procedures and computer systems to effectively carry out our mandate under the Solid Waste-Resource Management Regulations.

We recognize that there are, and will be, areas that need improvement. We appreciate the efforts of the Auditor General to identify those areas and to make positive suggestions for change. The process of implementing the recommended changes has already begun and will be completed in a timely fashion.

The RRFB Board and management have attempted to operate the company as efficiently and effectively as possible. The goal is always to maximize the net revenues available to municipalities and thereby reward them for helping the Province achieve its goal of 50% diversion by the year 2000. The roles, powers and responsibilities of the RRFB and the Department of Environment must be clearly defined to ensure all revenues are collected when due. Inconsistencies that frustrate the efforts of both parties to maximize revenues, such as the Harmonized Sales Tax on beverage containers, must be eliminated. The RRFB supports the recommendations of the Auditor General in both these areas.

The RRFB has stepped up its audits of beverage distributors and tire retailers to ensure compliance with the ***Environment Act*** *and the Solid Waste-Resource Management Regulations. RRFB staff and DOE officials are meeting to clarify the responsibility for compliance enforcement under the legislation and regulations.*

The Board and management of RRFB have taken a proactive approach to management of the company. We must ensure that our policies, practices and procedures support the initiatives of the Province, the municipalities and of all Nova Scotians in treating solid waste as a valuable resource.

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 listing 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 those crown corporations and agencies audited by the private sector. This chapter of our Report contains comments on audits conducted by the private sector and by this Office.

AUDITS BY THE PRIVATE SECTOR

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

- there was any indication of inadequate controls or accounting records in the auditor's letter to management or audit opinion;
- 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 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 one corporation.

17.6 *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, net earnings would have decreased by $3.4 million, the opening deficit would have been reduced by $6.8 million, and unamortized foreign exchange losses carried forward would be $3.4 million.

Financial Controls and Records

17.7 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. Although most were not serious enough to include in this Report, observations in letters to management at the Nova Scotia Liquor Commission, Queen Elizabeth II Health Sciences Centre, Waterfront Development Corporation Limited, and the Workers' Compensation Board of Nova Scotia are appropriate to report.

- The auditors of the Nova Scotia Liquor Commission noted weaknesses in control over high turnover inventory items and weaknesses in accounts payable reconciliation procedures. Weaknesses were also noted in information system security and access, documentation and data integrity. In addition, the auditors identified the need for clarification of responsibilities in the Memorandum of Understanding between the Department of the Environment and the Commission pertaining to the Resource Recovery Fund.

- The auditors of the Queen Elizabeth II Health Sciences Centre reported weaknesses in controls over accounts receivable, research projects and leased equipment. In addition, the auditors noted weaknesses relating to computer password control, user access privileges and virus protection software. Other findings reported by the Centre's auditors are included in Chapter 15 of this Report, page 169.

- The auditors of the Waterfront Development Corporation Limited noted a lack of adequate general ledger reconciliation procedures and weaknesses in control over parking revenues.

- The auditors of the Workers' Compensation Board of Nova Scotia noted that the Province of Nova Scotia has agreed to guarantee the Board a real rate of return on the Board's invested assets. Although the guarantee is a key assumption used in the actuarial valuation of the Board's benefit liabilities, the understanding with the Province has not been formalized with a signed agreement. The auditors also reported weaknesses in control over accounts payable.

Timeliness of Financial Reporting and Release of Management Letters

17.8 Preparation, audit and release of financial statements and related management letters within six months of year-end are considered to be satisfactory. The financial statements for Nova Scotia Power Finance Corporation had not been audited and released by the time of our review assignment, approximately eight months after year-end.

17.9 As of December 1997, the audit of Sydney Steel Corporation had not been completed and financial statements had not been released for the year ended December 31, 1996. The status of certain matters pertinent to the *Joint Operation, Sale and Long-Term Agreement* between the Province and China National Metals & Minerals Import and Export Corporation, particularly those related to the fulfilment of obligations by the Province, have not been resolved. Last year we reported that the audit of the 1995 financial statements was not completed for the same reason. As of the writing of our Annual Report, the 1995 audit has yet to be finalized.

17.10 As a consequence, the financial statements of Sydney Steel Corporation are not included in the March 31, 1997 *Public Accounts of the Province of Nova Scotia*. The 1997 *Public Accounts* includes draft unapproved financial statements for the Nova Scotia Power Finance Corporation.

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 shown 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 of the Province Nova Scotia* present the financial position and operating results of all entities which are owned or controlled by government.

17.14 In addition to Sydney Steel Corporation, referred to above, the March 31, 1997 *Public Accounts* do not contain the annual financial statements prepared for the following government-controlled entities:

Halifax-Dartmouth Bridge Commission
Nova Scotia Credit Union Deposit Insurance Corporation
Sydney Tar Ponds Clean-Up Inc.
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 THIS OFFICE

17.16 The following observations resulted from audit assignments 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 26 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 This year there was only one case where it was necessary for our Office to express a qualification of opinion.

17.19 *Nova Scotia Gaming Corporation* - As a result of our audit we qualified our opinion on the March 31, 1997 financial statements as follows:

> "*The Nova Scotia Gaming Corporation has prepared the financial statements as they relate to casino gaming based upon their interpretation of the Operating Contract between the*

Corporation and Metropolitan Entertainment Group. This interpretation results in the adoption of an expense allocation approach which recognizes the payment of the shortfalls that arose in the previous year referred to in Note 3(h) to the Corporation's financial statements as an expense for the current year. In my opinion, the amounts that represent these shortfalls are expenses which should be recognized in the year incurred. If these shortfalls had been recognized as expenses in the previous year, net income of the Corporation reported for that year would have been reduced by $2,143,409 and net income of the Corporation being reported for the current year would have been increased by $2,143,409."

17.20 Note 3(h) to the financial statements states:

"*During the previous year, the income was insufficient to allocate to the Operator the maximum allocation to which the Operator was entitled with reference to their capital investment (Note 3e). The Operator's accumulated shortfall as at March 31, 1996, which has been eliminated, totalled $459,799 in Halifax and $1,683,610 in Sydney. These amounts were allocated to the Operator from income during the year ended March 31, 1997 and accordingly were recorded as expenses of the Corporation in the current year*."

System Weaknesses

17.21 We noted situations during our audits where accounting and financial 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 report to the House of Assembly.

17.22 *Insured Prescription Drug Plan Trust Fund* - Maritime Medical Care Inc. administers the Pharmacare Program on behalf of the Department of Health and the Seniors' Pharmacare Board. Our financial statement audit resulted in several recommendations for improvements in the Program administrative controls at Maritime Medical Care Inc. which were reported in the management letter issued to the Seniors' Pharmacare Board at the conclusion of the audit. These recommendations included:

- more frequent reconciliations of general ledger control accounts and sub-ledgers;
- improvements in the process for monitoring overdue accounts;
- improvements in the process for verification of seniors' income when determining eligibility for the low income credit;
- improvements to controls over the cash receipts function including more timely depositing of cheques received from seniors; and
- the need for better control of password access to computerized accounting systems.

17.23 Subsequent to the audit, we were advised by Maritime Medical Care Inc. that all of the above recommendations had been implemented.

17.24 In addition, we noted that the Seniors' Pharmacare Board and the Department of Health prepared projections for the Seniors' Pharmacare Program for the 1996-97 fiscal year but did not approve a budget. We have recommended that a budget for revenues and expenditures be approved by the Board and the Department of Health prior to the start of each fiscal year. Budgeted revenues and expenditures should be disclosed in the annual audited financial statements to facilitate comparison of actual performance in relation to budget and analysis of associated variances.

17.25 *Nova Scotia Business Development Corporation* - We noted that staff of the Department of Economic Development and Tourism posted entries to revise the reserve balances of the Nova Scotia Business Development Corporation Fund and the Industrial Expansion Fund. The amount of the entries was not supported by any analysis and did not agree with the Corporation's assessments. Adjustments to the reserve balances should only be initiated by staff of the Corporation, and only after an analysis of the account portfolio has been completed and the Board of Directors is satisfied with the amount of reserve to record. We were also told that formal recommendations concerning the Industrial Expansion Fund are being made to Executive Council by Department officials without staff of the Corporation being informed on a timely basis.

17.26 *Nova Scotia Film Development Corporation* - We noted that the Corporation's listings of equity investments and development loans were incomplete and inaccurate. We recommended that procedures be established to ensure the completeness and accuracy of these records. We also recommended that long-term strategies and plans be developed for the Corporation's audit of recipients of assistance. Such strategies should include a regular review of the spending of Film Development Corporation assistance to ensure it was used for the purposes intended.

17.27 *Nova Scotia Grain and Forage Commission* - Effective August 6, 1997, the government entered into an agreement to facilitate the transfer of the Commission's operations to a private trust. We noted that the agreement did not specifically address the transfer of the cash, accounts receivable and liabilities of the Commission. We also observed that Goods and Services Tax owing from July 31, 1995 had not yet been remitted to the Federal government.

17.28 *Nova Scotia Hospital* - We noted that programming changes to the computerized inventory system were tested against a transaction file containing "live" (i.e., actual) Hospital data. We found no material errors in the financial statements due to this weakness, but it could potentially lead to material errors. We recommended that programming changes be made in a test environment, using a file set up in the system containing data for testing purposes only.

17.29 *Housing Development Fund* - Last year we reported accounting and control weaknesses within the system used to capitalize interest costs to land development projects. We also noted the need to implement a process of scheduled, periodic assessments of land holdings to ensure the accurate valuation of land development projects in the financial statements of the Fund. During our 1997 audit we noted similar weaknesses in the systems of control and repeated our recommendations to the Department of Housing and Municipal Affairs.

17.30 *Nova Scotia Innovation Corporation* - We noted that the Board of Directors approved, in general terms, the investment by the Corporation in another enterprise. However, details such as the percentage ownership, funds involved and the method of investment were not reviewed and approved by the Board. In our view, the Board should give final approval to the details of investments made by the Corporation.

Legislative and Policy Compliance Weaknesses

17.31 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 should be brought to the attention of the House of Assembly.

17.32 *Fisheries and Aquaculture Development Fund* - The Fisheries and Coastal Resources Act (Part IV, Section 37) states "*All repayments and all recoveries made in respect of any transaction out of the Fund shall be credited to the Fund.*" It has been the Nova Scotia Fisheries and Aquaculture Loan Board's practice to reduce the balance of the Fund when loans are written off.

However, we understand that subsequent recoveries are credited to the Province's consolidated fund, and not to the Fisheries and Aquaculture Development Fund.

17.33 *Nova Scotia Business Development Corporation* - We noted that the Property Management Committee, a committee of the Board of Directors, had approved a property transaction for which it did not have approval authority. The Board of Directors should approve transactions outside the Committee's jurisdiction or the delegated authority levels should be revised.

17.34 *Nova Scotia Hospital* - As we reported last year, 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.

17.35 *Housing Development Corporation* - The Corporation guarantees loans under Section 9(d) of the Housing Development Corporation Act. However, the Corporation has not made the required reports to the Minister of Finance and received appropriate Governor in Council approval for guarantees made, as required under Section 59(4) of the Provincial Finance Act. This section of the Provincial Finance Act was enacted in 1994. Department staff were not aware of the amendment to the Act until recently. Department staff informed us that guarantees are now being submitted to the Governor in Council for approval.

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. There was one delay this year resulting from a lack of readiness by the auditee.

17.37 *Housing Development Fund and Corporation* - The financial statements and related management letters of the Housing Development Fund and Housing Development Corporation for the year ended March 31, 1997 were not released until late in the fall of 1997. Delays were due primarily to problems in the implementation of changes to accounting policies for profit recognition on land sales. We recommended that sufficient, appropriate resources be devoted to the accounting function so that financial statements can be issued on a timely basis in future years.

OTHER AUDIT OBSERVATIONS

18.

ADDITIONAL APPROPRIATIONS

BACKGROUND

18.1 Every year the *Estimates*, representing the government's spending plans, are presented to the House of Assembly for review and approval. The *Estimates* are summarized in the Appropriations Act, which authorizes spending amounts (or votes) for the coming year.

18.2 The Provincial Finance Act allows adjustments to these spending plans in the form of additional appropriations. The Provincial Finance Act also permits the Executive Council to approve special warrants when an expenditure, which was not provided for in the original *Estimates*, is urgently and immediately required.

18.3 The Expenditure Control Act Section 12(2) provides "*Notwithstanding subsection (1), an amount may be expended in a fiscal year for net capital expenditures and net program operating expenditures that is no more than one percent more than the amount appropriated by the Legislature for those expenditures.*" Section 13 of the Expenditure Control Act requires that expenditures in excess of the one percent threshold "*may only be made after a resolution has been passed by the House of Assembly authorizing the expenditure.*" For purposes of this chapter, the additional amounts approved by resolution of the House under Section 13 of the Expenditure Control Act are included as additional appropriations.

18.4 Exhibit 18.1 on page 201 includes sections of the Provincial Finance Act relating to additional appropriations and special warrants. Exhibit 18.2 on page 202 includes sections of the Expenditure Control Act which are applicable to the 1996-97 fiscal year.

18.5 Finance's current practice is that, when forecasting indicates an expenditure vote may be exceeded, it works with the affected department to identify alternatives and opportunities to avoid the overexpenditure situation. Depending on the circumstances, an additional appropriation may be necessary. Further, it was indicated by Finance that they wait to obtain an additional appropriation until they know with a high degree of certainty the amount of an additional appropriation. This avoids seeking further appropriations for minor amounts.

18.6 Finance also indicated that they are reluctant to seek spending approvals greater than the original budget estimate when there is a good probability that departmental spending pressures can be managed down to the original budgetary limit.

18.7 Section 9(2)(e) of the Provincial Finance Act requires that the *Public Accounts* include a summary listing of additional appropriations and special warrants for the fiscal year authorized under Sections 28 and 29 of that Act. Under Section 9(1) of the Auditor General Act, we are required to call attention to every case in which an appropriation was exceeded, and every case in which a special warrant was made pursuant to the provisions of the Provincial Finance Act.

RESULTS IN BRIEF

18.8 The following are the principal results from our 1997 review of additional appropriations and special warrants.

- The timing of approvals of additional appropriations continues to be a concern. All additional appropriations for the 1996-97 fiscal year were approved by either the Executive Council or the House of Assembly. However, most of the related expenditures had been incurred before the approvals were received.
- There were additional appropriations totalling $164,284,181 for the fiscal year ended March 31, 1997. Of these, additional appropriations totalling $164,156,181 were approved subsequent to March 31, 1997, after the overexpenditures had been incurred.
- There were no special warrants approved for the 1996-97 fiscal year.

SCOPE OF REVIEW

18.9 The objective of our annual review of additional appropriations and special warrants is to determine if they were properly authorized in accordance with the provisions of the Provincial Finance Act and where appropriate, the Expenditure Control Act.

18.10 In addition to reviewing the supporting information obtained from Finance, we also performed a search of Orders in Council and resolutions of the House of Assembly to verify completeness of the listing of additional appropriations and special warrants to be published in the *Public Accounts*.

PRINCIPAL FINDINGS

Additional Appropriations

18.11 The Appropriations Act, 1996 contained 37 votes for expenditures totalling $4,515 million (including sinking fund instalments and serial retirements of $217.4 million).

18.12 All additional appropriations for the 1996-97 fiscal year were approved by either the Executive Council or the House of Assembly. However, most of the related expenditures had been incurred before the approvals were received, which in our view may be contrary to the Provincial Finance Act and the Expenditure Control Act.

18.13 Additional appropriations were approved by the Executive Council under the provisions of Sections 27A and 28 of the Provincial Finance Act on February 25, 1997, April 22, 1997 and September 17, 1997. Further, a resolution in the House of Assembly, under the provisions of the Expenditure Control Act, was submitted to the House on April 22, 1997 and approved on April 28, 1997.

18.14 There were additional appropriations totalling $164,284,181 approved for the fiscal year ended March 31, 1997. Of these, additional appropriations totalling $164,156,181 were approved subsequent to the year-end, after the overexpenditures had been incurred.

18.15 Our review noted that the four departments listed below accounted for approximately 99.6% of the total additional appropriations for 1996-97.

	($ millions)
Community Services	$ 5.5
Education and Culture	15.3
Health	124.1
Housing and Municipal Affairs	3.1
Justice	15.4
	$163.4

18.16 More specific details of additional appropriations for three of the four departments are as follows.

- **Education** - Additional funds were required by Education and Culture mainly because of the decision to record advances made to private sector consortia building public-private partnership schools as part of the capital assets of the Province (see page 78). The additional appropriation was approved by OIC on April 22, 1997.

- **Justice** - Additional funding required by Justice was primarily due to increases in the Compensation for Victims of Institutional Abuse Program. The additional appropriation was approved by resolution in the House of Assembly on April 28, 1997.

- **Health** - The Department of Health required additional funding in the areas of Acute Care, Out-of-Province Claims, Medical Society increase in Medical Payments and uncollectible accounts receivable. The additional appropriations were approved by resolution in the House of Assembly on April 28, 1997.

18.17 The following is a summary of additional appropriations for the last ten years.

Additional Appropriations
($ millions)

Year	Current	% of Estimate	Capital	% of Estimate	Total
1996-97	$ 142.3	3.2%	$ 22.0	13.8%	$164.3
1995-96	140.6	3.4%	1.5	0.5%	142.1
1994-95	51.2	1.2%	1.6	0.5%	52.8
1993-94	33.5	0.7%	8.0	2.4%	41.4
1992-93	118.5	2.7%	26.0	8.8%	144.5
1991-92	86.3	2.0%	3.2	1.2%	89.5
1990-91	77.0	1.9%	3.3	1.1%	80.3
1989-90	126.3	3.3%	32.6	9.3%	158.9
1988-89	87.6	2.5%	16.8	12.2%	104.4
1987-88	50.4	1.5%	8.4	5.4%	58.8

18.18 The following is a list of additional appropriations of $50,000 or greater, representing 99.9% of the $164,284,181 approved for the year ended March 31, 1997. A complete listing is included in Volume I of the Province's *Public Accounts*.

Additional Appropriations
$50,000 or Greater

Department	Date Approved	Authorized
Approved by OIC		
Agriculture and Marketing	Feb. 25, 1997	$ (91,000)
Business and Consumer Services	Feb. 25, 1997	(546,000)
Community Services	Apr. 22, 1997	5,503,000
Education and Culture	Apr. 22, 1997	15,336,000
Finance	Feb. 25, 1997	243,000
Fisheries	Feb. 25, 1997	(86,000)
Housing and Municipal Affairs	Feb. 25, 1997	308,000
Housing and Municipal Affairs	Apr. 22, 1997	2,867,000
Natural Resources	Feb. 25, 1997	220,000
Public Service		
Human Rights Commission	Sept. 17, 1997	202,317
Public Inquiry, Westray Mine	Apr. 22, 1997	750,000
The Nova Scotia Economic Renewal Agency	Feb. 25, 1997	371,000
Transportation and Public Works	Feb. 25, 1997	(276,000)
Approved by Resolution in the House		
Health	Apr. 28, 1997	124,115,000
Justice	Apr. 28, 1997	15,364,000
		164,280,317
Additional appropriations less than $50,000 (net)		3,864
		$164,284,181

Special Warrants

18.19 We are required under Section 9(1)(f) of the Auditor General Act to call attention to every case in which *"a special warrant, made pursuant to the provisions of the Provincial Finance Act, authorized the payment of money."* The Provincial Finance Act allows the Governor in Council to approve a special warrant, when the Legislature is not in session, which authorizes *"an expenditure which was not provided for by the Legislature"* and *"is urgently and immediately required for the public good."*

18.20 There were no special warrants approved for the 1996-97 fiscal year.

Concluding Remarks

18.21 Expenditure of funds beyond the votes or appropriations approved by the House of Assembly continues to occur prior to the Governor in Council approval required under the Provincial Finance Act or the passing of a resolution by the House of Assembly under the Expenditure Control Act.

18.22 Current legislation and administrative practices raise questions as to the effectiveness of the House of Assembly's control over expenditure of public funds. The practice of obtaining after-the-fact approval for additional appropriations, while possibly more efficient, does not necessarily constitute *effective control* and, we believe, contravenes the intent of the requirements of the Provincial Finance Act and the Expenditure Control Act.

18.23 It is the stated intention of the Department of Finance to identify opportunities to enhance efficiency in order to support effective control over appropriations. In this regard, there may be modifications to the Expenditure Control Act and the Provincial Finance Act that could be made to enhance efficiency, while maintaining effective control. We have agreed to participate with Finance in a review of the policies and practices in other jurisdictions for the use and control of additional appropriations.

Exhibit 18.1

EXTRACTS FROM THE PROVINCIAL FINANCE ACT

Prerequisite to issue of money
13(2) *The Deputy Minister* [of Finance], *or an officer designated by him, before the issue of public money out of the Consolidated Fund, shall ensure that there is sufficient balance available in the appropriation for the specified purpose.*

Consequence of exhausted appropriation
13(3) *When an appropriation is exhausted, the Deputy Minister shall forthwith notify the department to which the appropriation was granted and the Minister, and shall not sanction any further contractual obligations or commitments to be charged to the exhausted appropriation.*

Suspension of right to commit
27(A) The Governor in Council, upon the recommendation of the Minister, may order the suspension for such a period as the Minister deems fit of the right to commit any appropriation or part thereof except the salaries, wages and expenses of members of the public service, including the civil service, or the indemnities and expenses of the members of the House of Assembly.

Report of insufficient appropriation
28(1) *When it appears to the Minister or principal officer having charge of a service that the sum appropriated by the Legislature for an ordinary or usual service is insufficient to meet the requirements of that service during the year for which the appropriation has been made or that the sum appropriated by the Legislature to be expended on capital account is insufficient for the service for which it was appropriated, the Minister or principal officer shall make a report of that fact to the Minister of Finance and shall in such report estimate the additional sum required to carry out the service.*

Supplementary appropriation
28(2) *Upon the receipt of such report, the Minister of Finance may make a report to the Governor in Council showing the need of additional appropriation and thereupon the Governor in Council may order that such additional sums as are deemed necessary for the said service be appropriated accordingly, provided that the additional sums appropriated to be expended on capital account shall not exceed twenty-five per cent of the amount appropriated by the Legislature for the service.*

Report of urgently required expenditure
29(1) When it appears that an expenditure which was not provided for by the Legislature is urgently and immediately required for the public good, the head of the department concerned shall make a report of that fact to the Minister of Finance and shall in such report estimate the amount of the proposed expenditure.

Special warrant
29(2) Upon receipt of such report, the Minister may make a report to the Governor in Council that the said expenditure is urgently and immediately required for the public good, and that there is no legislative provision therefor, and the Governor in Council may thereupon order a special warrant to be prepared to be signed by the Lieutenant Governor for the issue of the amount estimated to be required, and may order the amount to be charged to Capital Account or to Current Account, or partly in one way and partly in the other.

Conditions for special warrant while house in session
29(3) A special warrant pursuant to the provisions of this Section shall not be made when the Legislature is in session unless the House of Assembly has not sat for any of the five days immediately preceding the issue of the special warrant.

Exhibit 18.2

EXTRACTS FROM EXPENDITURE CONTROL ACT

Application of Part II

11 For greater certainty, this Part applies to the 1996-97 and subsequent fiscal years of the Province.

Expenditure reductions for 1996-97
12(1) In each and every fiscal year of the Province commencing with the 1996-97 fiscal year, the amount appropriated by the Legislature for net capital expenditures and net program operating expenditures shall not exceed the amount of revenue forecast to be received by the Minister for that fiscal year.

Expenditure exception
12(2) Notwithstanding subsection (1), an amount may be expended in a fiscal year for net capital expenditures and net program operating expenditures that is no more than one percent more than the amount appropriated by the Legislature for those expenditures.

Time limit for recovery of deficit
12(3) Where net capital expenditures and net program operating expenditures for a fiscal year exceed the total revenues for that year, the resulting deficit shall be recovered no later than the end of the second fiscal year following the fiscal year in which the deficit occurred by a reduction in expenditures or an increase in revenue, or both, over that period.

Use of surplus
12(4) Where the amount of revenue to be received by the Minister in a fiscal year exceeds the amount appropriated by the Legislature for net capital expenditures and net program operating expenditures for that year, the resulting surplus shall, after accounting for any recoveries required pursuant to subsection (3), be used to reduce the public debt of the Province or reduce taxes, or both.

Resolution of House
13 Where net capital expenditures and net program operating expenditures for a fiscal year exceed the amount authorized to be spent pursuant to Section 12, the expenditures in excess of the amount authorized by subsection 12(1) and (2) may only be made after a resolution has been passed by the House of Assembly authorizing the expenditure.

19.

CASH AND OTHER LOSSES

BACKGROUND

19.1 The Government of Nova Scotia Management Manual 200, Chapter 8 requires that departments, boards, or commissions immediately report any instances of loss of public money or public property to the Department of Finance, and to the Office of the Auditor General. Finance is responsible for establishing procedures to be followed for the reporting of any irregularities or losses.

19.2 Section 9(1)(e) of the Auditor General Act requires that we report annually every case observed where there has been a deficiency or loss through fraud, default or mistake of any person. This chapter summarizes the losses identified by or reported to us.

RESULTS IN BRIEF

19.3 The following summarizes our principal findings from our 1997 review.

- The losses reported to us for the year ended March 31, 1997 totaled $293,415; consisting of cash losses of $24,482, property losses estimated at $314,535 and recoveries of $45,602.
- Most, but not all, departments and crown agencies are complying on a timely basis with the loss reporting requirements of the Management Manual.
- As suggested in previous Reports, Finance has reviewed and clarified the policies and practices for the reporting of losses.

SCOPE OF REVIEW

19.4 Our objective was to review the information provided by departments and agencies, and compile a summary listing of the cash and property losses reported to us for the year ended March 31, 1997.

19.5 We sent letters to departments and crown agencies to confirm the completeness of the losses reported to us. In recognition of the fact that departments and agencies may be able to recover some of their losses, we asked that specific recoveries be reported as well. Further, we have performed no additional or specific audit procedures on the losses reported.

19.6 This review did not consider the losses which resulted from write-offs of uncollectible receivables or advances approved annually by Executive Council.

PRINCIPAL FINDINGS

Losses Reported

19.7 The following is a summary of the cash and property losses for the year ended March 31, 1997 identified either as a result of our confirmation request or reported to us during the year. Certain of the losses reported represent the entity's estimated value of property lost or damaged.

Departments Reporting Losses	Cash	Property	Recoveries	Total
Transportation and Public Works	$ -	$ 93,336	$ (10,200)	$ 83,136
Community Services	12,354	1,600	(12,354)	1,600
Fisheries	-	3,765	-	3,765
Education and Culture	5,815	-	-	5,815
Environment	390	28,000	(16,629)	11,761
Health	9	5,164	-	5,173
Justice	204	4,200	-	4,404
Natural Resources	4,542	24,603	-	29,145
Business and Consumer Services	320	300	-	620
Housing and Municipal Affairs	731	14,000	-	14,731
Economic Development and Tourism	-	4,300	-	4,300
	24,365	179,268	(39,183)	164,450
Crown Agencies Reporting Losses				
Nova Scotia Hospital	117	700	-	817
Nova Scotia Liquor Commission	-	120,860	-	120,860
Workers' Compensation Board of Nova Scotia	-	2,448	-	2,448
Nova Scotia Legal Aid Commission	-	259	-	259
Sydney Steel Corporation	-	11,000	(6,419)	4,581
	117	135,267	(6,419)	128,965
Total Reported	$ 24,482	$ 314,535	$ (45,602)	$ 293,415

19.8 The above table is not complete as not all departments and crown agencies have included values for property items which have been lost, damaged or destroyed. For example, the Department of Justice reported that, based on information in its fixed asset inventory system, 20 items have been misplaced, and there was no dollar value reported for those items. Justice is the only government entity reporting these types of losses, and we believe other entities should be required to do so. Further, the Nova Scotia Alcohol and Gaming Authority (NSAGA) reported the loss of a cellular phone, but did not provide information on the cost or estimated value of the lost item.

19.9 In regards to the Nova Scotia Liquor Commission, it should be acknowledged that it is a retail organization and not a government department. As such, it is subject to different risks of losses. As a self-service retail organization, it is inevitable that some inventory shrinkage will occur. The property losses reported for the Nova Scotia Liquor Commission represent the cost of inventory stock losses from its retail and warehouse operations.

Compliance with Reporting Requirements

19.10 All entities are not complying with the requirement to report losses on a timely basis to Finance and this Office. Failure by some entities to report consistently and on a timely basis restricts Finance's ability to ensure that necessary follow-up procedures are performed to determine the reason for a loss and whether appropriate corrective action has been taken.

19.11 Subsequent to March 31, 1997, Finance took steps intended to support improved and more consistent compliance by departments and agencies with the defined policy and procedures. Finance also clarified the value to be used in reporting losses as the Management Manual does not specify this. Further, the internal audit division at Finance now investigates losses reported to determine whether steps have been taken to prevent such losses from occurring in the future.

CONCLUDING REMARKS

19.12 None of the specific losses reported to us with respect to the 1996-97 fiscal year appear to be of such significance (i.e., due to the nature, circumstances or size of the losses) that they warrant further or special attention by this Office at this time. We will consider the results of the Department of Finance internal audit group’s work on these reported losses as part of our 1998 review.

20.

CLAIMS UNDER FEDERAL-PROVINCIAL AGREEMENTS

INTRODUCTION

20.1 The Province has entered into a number of agreements with the Government of Canada for various cost-shared programs. Our Office has the responsibility to audit programs and sub-programs under certain of these agreements. For the year ended March 31, 1997, we commenced audits of claims under ten separate agreements (although not all of these audits were completed at the time of writing this Report). The agreements were administered by five government departments and two Provincial agencies. Total expenditures under these agreements amounted to $113 million, of which $62 million was recoverable from the Government of Canada. Since our last Report we also finalized the audits of claims under four separate agreements for the year ended March 31, 1996.

20.2 Our responsibility is to determine whether the departments and agencies concerned have complied with the terms of the agreements and whether the amounts incurred and claimed are in accordance with the agreements. We also review and evaluate the systems used to control the processing of expenditures under the agreements.

PRINCIPAL FINDINGS

Reservation of Opinion

20.3 This year there were two cases where it was necessary to express reservations of opinion.

20.4 *Canada/Nova Scotia Development Fund Agreement* - Consulting and Audit Canada (CAC) is contracted by Natural Resources Canada to conduct an annual audit of expenditures incurred under this agreement. We qualified our audit opinion on the 1995-96 fiscal year claim because the Management Committee responsible for the agreement had not determined whether they would accept the adjustments recommended in the audit report prepared by CAC for the year ended March 31, 1996.

20.5 *Agreement on Social Housing* - Sponsors under the Private Non-Profit Housing Program are required to verify income and calculate rents using guidelines and a rent-to-income (RGI) scale contained in the Non-Profit Housing Operations Manual. We qualified our audit opinion on the claim for this Program because auditors of two project sponsors, upon which we rely to support our audit opinion, either did not express an opinion or did not conclude that the rent-to-income (RGI) scale was applied correctly by project sponsors.

20.6 We qualified our audit opinions on the Public Non-Profit Lease Purchase Housing Program and the Rent Supplement Housing Program claims because internal audit staff of the Department of Housing and Municipal Affairs, upon which we rely to support our audit opinion, did not perform sufficient audit work with respect to these Programs.

20.7 The Rural and Native Housing Group of Nova Scotia provided program grants under the Residential Rehabilitation Assistance Program (RRAP). We qualified our audit opinion on RRAP subsidy claims because an internal audit conducted by staff of the Department of Housing and Municipal Affairs, upon which we rely to support our audit opinion, concluded that there were insufficient inspections and documentation to support payments made to grant recipients. We also qualified the claims because the Department was unable to reconcile the advances and revenues recorded on the claims to the Department's general ledger.

Client Readiness

20.8 We consider client readiness to be a critical factor in the timely completion of claims audits. We encountered difficulties in completing the audits of three claims.

20.9 *Agreements on Canada Assistance Plan and Vocational Rehabilitation of Disabled Persons* - We have not finalized the audits of the claims under these two agreements for the fiscal year ended March 31, 1996 because we are awaiting information from Department of Community Services staff.

20.10 *Agreement on Social Housing* - Much of the documentation that we requested was not available to us at the start of the audit. Three of the ten claims we are required to audit had not been prepared by that date. Numerous adjustments to the claims were identified by our audit. The delays in completing the audit caused us to commit additional time beyond that which was budgeted and to request a deadline extension from Canada Mortgage and Housing Corporation.

Other Findings

20.11 We found certain situations during our claims audits where accounting systems and procedures were deficient. Although they were not of a magnitude to require a reservation of opinion, two such situations are significant enough to report to the House of Assembly.

20.12 *Canada/Nova Scotia Development Fund Agreement* - Under the Industrial Assistance - Shipyard Assistance Program, applicants are required to fund 25% of the total project cost by means of internal funding or a repayable loan from the Province. The Province is required to spend a sum equivalent to the repaid portion of the loans on additional infrastructure projects. The Management Committee responsible for the agreement has not resolved a number of issues related to the Program. These issues relate to the write-off of amounts owed to the Province, whether interest received on these loans should be returned to the Fund to reduce the total cost of the program, and how the proceeds of the potential sale of two shipyards will be allocated between the Province and the Fund.

20.13 *Agreement on Social Housing* - Under the Non-Profit Housing Program, project sponsors are required to submit financial statements. Not all external auditors of the sponsors are expressing an audit opinion on the application of the RGI scale as required by their audit engagement. The Department does not have a formal system in place to ensure all financial statements are received and adjustments to subsidies paid are processed on a timely basis.

OFFICE OF THE AUDITOR GENERAL

21.

REPORT ON THE OFFICE OF THE AUDITOR GENERAL

MANDATE

21.1 The responsibilities and authorities of the Auditor General are derived from the Auditor General Act (Chapter 28, 1989). The Act specifies the responsibility to examine the accounts of the Province and its various agencies and the requirement to report to the House of Assembly on the government's stewardship of public funds. Appendix I on page 222 of this Report includes extracts of the audit mandate and reporting sections of the Auditor General Act.

21.2 Some other Provincial statutes and regulations, as well as other enabling arrangements for certain entities, provide additional or more specific mandates to this Office. For the most part these relate to the performance of the annual financial statement audit function for certain crown agencies or funds. The Office's mandate under Section 65A of the Provincial Finance Act, with respect to the review of the annual revenue estimates, is quite unique.

21.3 In addition to the Office's statutory mandate(s) there have been instances where audit coverage by this Office has been incorporated into policy guidelines and control standards prepared by senior public servants. For example, see the extracts in Appendix 21A on page 219 from internal policy and standard guidelines. Further, the Department of Finance's draft policy for debt management also includes reference to specific involvement by this Office.

21.4 While we do not take exception to general reference to the Office's work in such policy statements, we are concerned that there may be some misunderstanding about the nature, extent or timing of our coverage in such regards. As presented, it could be interpreted that this Office actively audits each of the respective areas or matters on a detailed and almost continuing basis. This may not be the case, since each year we make decisions as to which aspects of government operations and control will get specific attention.

MISSION, VISION AND VALUES

21.5 Exhibit 21.1 is an extract from the Office's *Business Plan* which was prepared after consideration of the guidelines issued within government for use by departments and agencies.

STRATEGIC GOALS AND OBJECTIVES

21.6 As a result of internal planning activities, the Office has identified the following key goals that are being used to guide our audit and related activities.

- To achieve positive change in the accountability for and management of public funds.
- To provide assurance on the credibility of financial statements and other representations in order to assist the House of Assembly to hold the government to account.

Exhibit 21.1

Office of the Auditor General
Mission, Vision and Values

Our Mission **-** The Office derives its mandate from the Auditor General Act (Chapter 28, 1989). The people of Nova Scotia, through their elected representatives, need assurance that their tax dollars are expended for the purposes intended. As the legislative auditor of the Province, the Office helps the House of Assembly to hold the government to account by providing opinions:

- on the credibility of financial statements and other government representations;
- concerning compliance with legislation, regulations, agreements, and policies;
- on the adequacy of control; and
- on the extent of due regard for economy and efficiency in the management of public funds.

In addition, the Office provides advice to assist in improving the accountability for, and the management of, public funds.

Our Vision - The Office strives for excellence in public sector management and value for money in the use of public funds.

Our Values - In pursuing our mission, we value our clients, our people, and our professionalism.

- We strive to provide quality service to the House of Assembly, its members, and other clients. We do this with initiative and commitment, employing state of the art knowledge, skills, and abilities. We seek to be progressive, encouraging leadership, intelligent risk-taking, and high standards of reliability.
- We treat each other with fairness and equality, communicating openly, honestly, and respectfully. We place great importance in career development, training, professional fulfilment, and quality of work life. We work together as a partnership, support staff and professionals, recognizing each person's unique contribution.
- We work to the highest standards of our profession, maintaining a relationship with the House of Assembly and the government that is confidential, independent, objective, and professional. We endeavor to be creative while remaining practical, economical, and efficient. We share our knowledge, values, ideas, and experiences within the Office, the government, and our profession.

- To strive for excellence through the pursuit of state-of-the-art knowledge, skills and abilities, and to work to the highest standards of our profession.

- To provide cost effective use of resources in support of the role and responsibilities of our Office.

21.7 These goals are reviewed each year and will continue to evolve. Further, we monitor our overall performance against these goals.

CORE BUSINESS FUNCTIONS

21.8 The Office conducts audits under the Auditor General Act and reports the results to the House of Assembly. The types of audits and reports provided are described in the Mission. However, for purposes of a more complete description, our business function is comprised of the following elements:

- In addition to the Auditor General Act, other legislation, including the Provincial Finance Act, specifies audit responsibilities. Under each of these our function is to provide information to the House of Assembly, and advice to both the government and managers of government entities.

- We perform assessments from which flow the provision of assurance, advice, recommendations and analyses.

- We identify and monitor emerging issues, and research developments and initiatives in other jurisdictions related to the management and control of public funds, in order to provide advice regarding opportunities for improvement.

- We support the Public Accounts Committee by providing information through briefings, research and by responding to queries.

OUTCOME MEASURES

21.9 While outcomes can only be measured through compilation and interpretation of data from various sources, for purposes of performance monitoring, we have identified the following outcome measures relating to the achievement of the Office's strategic goals and objectives.

- The degree to which positive change has occurred in the management of public funds. This can only be measured over time and requires benchmarking and subsequent comparison.

- The extent to which financial statements and other management representations are presented fairly, on a timely basis, and are considered useful as accountability reports. This also can only be measured over time and requires benchmarking and subsequent analysis.

- The extent of external recognition of the Office as an effective professional legislative audit function. This can be measured in a variety of ways including peer review, report user feedback, media analysis and professional recognition.

- The comparison of the costs of the Office to the costs of similar legislative and other audit organizations. Various cost comparisons can be developed and analyzed to measure Office performance.

21.10 We have begun to gather and consider general information against these outcome measures, and are committed to such being a more formal and integral element of our ongoing planning and performance management processes. Further, initiatives within the legislative audit community, particularly under the auspices of the Conference of Legislative Auditors (COLA), appear to have the potential for refinement of outcome measures for legislative audit offices. We will continue to participate in these efforts while striving to utilize those outcome measures we have identified.

ORGANIZATION

21.11 As at December 1997 we had 25 staff, one of whom was seconded to the Department of Education and Culture. Subject to the availability of funds, we outsource for specialist expertise and other audit resources on selected assignments.

21.12 Public funds of the Province of Nova Scotia are collected and expended through various departments and agencies. In order to effectively plan and manage the activities of the Office, we are organized into three teams each headed by a senior manager. Staff members are periodically rotated among the teams to provide career development opportunities, technical training, and to meet operational priorities. Each of the senior managers reports to the Auditor General, participates in the overall management of Office activities, has overall responsibility for a group of departments and agencies, and is the prime focus for communications with those organizations.

21.13 It is a responsibility of each senior manager to periodically review past and intended audit coverage of assigned portfolio departments and agencies. These reviews are to be consolidated into multi-year strategic and longer-range plans giving due consideration to the needs of the House of Assembly, intended themes for reporting, evaluation of risk factors, and availability of resources.

21.14 Exhibit 21.3 on page 218 provides summary financial information on the Office's operations. Staff costs consistently account for 80% or more of the Office's expenditures on an annual basis.

21.15 The Office's restructuring and downsizing initiatives are being supported in part by increased use of information technology resources, including an application obtained from the Federal Department of Public Works and Government Services Canada.

COMMITTEE OF INDEPENDENT ADVISORS

21.16 In 1994 an Independent Advisory Committee of senior members of the business and academic community was established. The terms of reference for the committee are provided in Exhibit 21.2 on page 217. Several other legislative auditors in Canada successfully use such an advisory committee.

21.17 The creation of this group and its participation have been positive initiatives, and we appreciate the open and insightful contributions it continues to make to our efforts to plan and manage the Office's activities and outputs.

PROFESSIONAL AFFILIATIONS AND ACTIVITIES

21.18 The Office strives to remain at the leading edge of legislative and other professional audit practices, and to share knowledge and experiences within those communities. We do this through participation in a variety of professional organizations including the following.

The Canadian Conference of Legislative Auditors

The Canadian Institute of Chartered Accountants (CICA)

CCAF-FCVI Inc.

The Certified General Accountants Association

The Information Systems Audit and Control Association

The Institute of Chartered Accountants of Nova Scotia (ICANS)

The Institute of Internal Auditors (IIA)

The Society of Management Accountants

21.19 Professional staff at all levels participate as members of committees, by providing input and commentary on research publications, and by attending various professional conferences, seminars and meetings.

PERFORMANCE

21.20 Overall, we are pleased with our achievements. Much remains to be done, but the following are examples of our accomplishments over the past year.

- The Public Accounts Committee continues to meet regularly and appears to appreciate the briefings and other assistance provided by our Office.
- We continue to be the only legislative audit office that provides an opinion on the government's annual revenue estimates and such a review was once again performed. Interest in the provision of this service has been expressed by other jurisdictions.
- Communications with central agencies, departments, other government agencies, professional organizations and the public have been maintained and enhanced. Outside counsel through the Independent Advisory Committee has been of great benefit.
- Staff development continues to be a priority, particularly in the area of information technology. The Office's decision, three years ago, to return to the CA training program was rewarded again in 1997 as one of our students qualified.
- We made increased use of external contract audit resources to meet our financial statement audit deadlines.
- The use, control and audit of information technology resources is of strategic importance to the performance of the Office. We have made significant investments

in recent years aimed at providing our staff with the resources, training and support processes needed. This will represent an ongoing and continuing commitment by the Office, and we are actively taking steps to monitor the results and payback of the related investments.

- We commenced a review of our audit methodology and practices, including consideration of the implication of the CICA's new standards for assurance engagements.

- We issued a Special Report on the Province's March 31, 1997 financial statements on August 22, 1997.

- Due to statutory changes requiring government to release the *Public Accounts* by December 31, we adjusted our audit timetable and schedule in order to have this year's Report ready for release approximately two months earlier than in prior years.

PRIORITIES

21.21 Strategic and long-range planning for the Office is to be based on an analysis of the Office's audit universe which was updated last year. This will give due consideration to the needs of the Legislature, areas of risk, major themes and, of course, availability of resources.

21.22 With the continuing development of the government's plans and priorities as described in *Government By Design,* the Office will focus its activities on relating its audit objectives to the government's priorities of economic renewal, social responsibility, cost-effective and client-focussed service, and fiscal stability.

21.23 On the administrative side, our priorities are to continue to operate within our expenditure control plan. This will entail filling certain vacancies that arise as a result of retirements or resignations with more junior professional staff.

21.24 Within these overall strategic priorities, our specific goals are the following:

- To improve the quality of our audits by utilizing contracted specialists when it is cost effective to do so and where funds are available.

- To improve the quality of external communication.

- To continue to provide appropriate support to the Public Accounts Committee and to seek ways in which we can provide the Committee with more timely information on issues and developments.

- To build on and expand the use of information technology as a means of optimizing the cost effectiveness of Office resources.

21.25 In addition to the above and the specific audit projects planned, we plan to:

- Arrange to have our financial statement audit practices assessed by the Institute of Chartered Accountants of Nova Scotia's Professional Standards Review program.

- Pursue opportunities to have our broader-scoped audit practices subject to a peer review by qualified and experienced representatives from legislative audit functions in other jurisdictions.

- Pursue opportunities to conduct joint or concurrent audits in selected areas with the legislative audit functions in other jurisdictions.

- Continue our participation in a Conference of Legislative Auditors' study group on performance management and reporting by the legislative audit function and expand our use of the various performance indicators which have been identified through the COLA study group.

- Make further scheduling adjustments such that the *Report of the Auditor General* can be ready for release within two to three weeks of the release of the *Public Accounts*.

- Continue progress toward implementation of any changes to our audit methodology and practices, including adhering to the CICA's new standards for assurance engagements.

- Participate in joint audit initiatives relating to the new corporate financial management system (CFMS) as well as debt management policies and practices. External specialist and other audit resources will be involved in each of these.

- Increase liaison and communication with the internal audit community within government, especially in relation to achieving cost-effective and continued audit coverage of:

    - adequacy of financial systems and controls, and

    - compliance with government's procurement policies and information technology standards.

- Provide constructive and timely advice and assistance to the Public Accounts Committee, the central agencies of government and various departments and agencies to strengthen and formalize accountability arrangements. To the extent appropriate this will include timely audit input and advice during the development of proposed improvements.

Exhibit 21.2

AUDITOR GENERAL OF NOVA SCOTIA
COMMITTEE OF INDEPENDENT ADVISORS

TERMS OF REFERENCE

OBJECTIVE

The role of the committee is to advise the Auditor General on issues facing the Office and to assist in promoting effective management of public funds and improved accountability.

More specifically the Committee will consider and advise on:

1. Initiatives designed to strengthen the professional competence, adherence to professional standards and overall effectiveness of the Office.

2. Technical and managerial issues arising from government-wide and departmental audits.

3. Accountability issues with particular regard to information published by the Government on financial and program performance.

4. Strategic and long-term operational objectives of the Office.

MEMBERSHIP

1. The Committee consists of no fewer than six and no more than eight senior members of the business and academic community selected for their knowledge and experience in the fields of management, finance, accounting and auditing in both the public and private sectors.

2. Members serve on a voluntary basis at the invitation of the Auditor General for a term of one year and are eligible for reappointment.

3. The Committee is chaired by the Auditor General with secretarial support provided by his Office.

MEETINGS

1. Meetings are held at least semi-annually at the call of the chair.

2. An agenda and briefing material are prepared by the Auditor General and circulated in advance of the meeting. Additional briefings are provided by staff of the Office.

Exhibit 21.3

OFFICE OF THE AUDITOR GENERAL
SUMMARY FINANCIAL INFORMATION

	1996-97 Estimate	**1996-97 Actual**	**1997-98 Estimate**
Salaries & Benefits	$ 1,588,000	$ 1,453,041	$ 1,486,400
Operating Costs			
- Travel	57,500	59,520	67,500
- Professional & special services	25,000	29,468	39,000
- Supplies & services	76,500	58,258	65,000
- Other (including IT related costs)	64,000	167,668	77,900
	223,000	314,914	249,400
Gross Expenditure	1,811,00	1,767,955	1,735,800
Less: Fees & other charges	(120,000)	(142,100)	(112,800)
Net Expenditures	$ 1,691,000	$ 1,625,855	$ 1,623,000

(1) During 1996-97, the Office reallocated certain staff costs to fund technology investments. Also during 1996-97, the Technology & Science Secretariat acquired information technology resources for the Office at a cost of $85,000, which are not included above.

(2) The costs associated with the Office's leased premises are not included above. Those costs - approximately $108,700 for 1996-97 - are reported by the Department of Transportation and Public Works.

Appendix 21A

<u>Extracted from Procurement Guidelines</u>

Audit

All procurement activities will be subject to such audit processes as may be determined appropriate by the Auditor General or the Auditor General in consultation with the Procurement Branch. Two forms of audit may occur. A compliance audit may be conducted to determine the level of adherence with established procurement rules and policies. A quality audit may also be undertaken in conjunction with or separately from compliance audits. The quality audit will examine the process undertaken and decisions reached from a defensibility and accountability point of view. Departments experiencing unacceptable compliance or quality audits and, in the opinion of the Minister of Finance, fail to undertake suitable measures for their resolution, may have all delegated procurement authority revoked until such time as satisfactory steps have been taken.

All procurement activities will be subject to audit by departmental internal auditors and specific audits as instructed by the Procurement Branch.

<u>Extracted from Information Technology (IT) Standards</u>

Review for Compliance:

Perform formal review of various departments' use of IT standards. Done by the Office of the Auditor General.

Audit Process and Report:

Produce formal audit report on departments' use of IT Standards. Done by the Office of the Auditor General.

Audit for Benefit and Value:

Perform audit of IT standards use in departments regarding the benefit and financial value. Done by the Office of the Auditor General.

APPENDICES

Appendix I

AUDITOR GENERAL ACT

SECTION 8

The Auditor General shall examine in such manner and to the extent he considers necessary such of the accounts of public money received or expended by or on behalf of the Province, and such of the accounts of money received or expended by the Province in trust for or on account of any government or person or for any special purposes or otherwise, including, unless the Governor in Council otherwise directs, any accounts of public or other money received or expended by any agency of government appointed to manage any department, service, property or business of the Province, and shall ascertain whether in his opinion

(a) accounts have been faithfully and properly kept;

(b) all public money has been fully accounted for, and the rules and procedures applied are sufficient to secure an effective check on the assessment, collection, and proper allocation of the capital and revenue receipts;

(c) money which is authorized to be expended by the Legislature has been expended without due regard to economy or efficiency;

(d) money has been expended for the purposes for which it was appropriated by the Legislature and the expenditures have been made as authorized; and

(e) essential records are maintained and the rules and procedures applied are sufficient to safeguard and control public property.

SECTION 9

(1) The Auditor General shall report annually to the House of Assembly the results of his examination and call attention to every case in which he has observed that

(a) any officer or employee has wilfully or negligently omitted to collect or receive any public money belonging to the Province;

(b) any public money was not duly accounted for and paid into the Consolidated Fund of the Province;

(c) any appropriation was exceeded or was applied to a purpose or in a manner not authorized by the Legislature;

(d) an expenditure was not authorized or was not properly vouched or certified;

(e) there has been a deficiency or loss through fraud, default or mistake of any person;

(f) a special warrant, made pursuant to the provisions of the *Provincial Finance Act*, authorized the payment of money; or

(g) money which is authorized to be expended by the Legislature has not been expended with due regard to economy and efficiency,

and to any other case that the Auditor General considers should be brought to the notice of the House of Assembly.

(2) The report of the Auditor General shall be laid before the House of Assembly on a day following the day upon which the Public Accounts have been laid before the House of Assembly.

(3) Whenever a case of the type described in clause (a), (b), or (e) of subsection (1) comes to the attention of the Auditor General, he shall forthwith report the circumstances of the case to the Minister.

(4) The Auditor General shall, as soon as practical, advise the appropriate officers or employees of an agency of government of any significant matter discovered in an audit.

(5) Notwithstanding subsection (1), the Auditor General is not required to report to the House of Assembly on any matter that the Auditor General considers immaterial or insignificant.

SECTION 15

Notwithstanding any provision of this Act, the Auditor General may, and where directed by the Governor in Council or the Management Board shall, make an examination and audit of

(a) the accounts of an agency of government; or

(b) the accounts in respect of financial assistance from the government or an agency of the government of a person or institution in any way receiving financial assistance from the government or an agency of government,

where

(c) the Auditor General has been provided with the funding the Auditor General considers necessary to undertake the examination and audit; and

(d) in the opinion of the Auditor General, the examination and audit will not unduly interfere with the other duties of the Office of the Auditor General pursuant to this Act,

and the Auditor General shall perform the examination and audit and report thereon.

SECTION 17

(1) Where the Governor in Council pursuant to this Act or any other Act has directed that the accounts of public money received or expended by any agency of government shall be examined by a chartered accountant or accountants other than the Auditor General, the chartered accountant or accountants shall

(a) deliver to the Auditor General immediately after the completion of the audit a copy of the report of findings and recommendations to management and a copy of the audited financial statements relating to the agency of government; and

(b) make available to the Auditor General, upon request, and upon reasonable notice, all working papers, schedules and other documentation relating to the audit or audits of the agency accounts.

(2) Notwithstanding that a chartered accountant or accountants other than the Auditor General have been directed to examine the accounts of an agency of government, the Auditor General may conduct such additional examination and investigation of the records and operations of the agency of government as he deems necessary.

Appendix II

CROWN CORPORATIONS, BOARDS, COMMISSIONS AND FUNDS

Financial Statement Audits Performed by Auditor General

Agricultural Organizations

- Gross Revenue Insurance Plan
- Nova Scotia Crop and Livestock Insurance Commission
- Nova Scotia Grain and Forage Commission
- Provincial Community Pasture Board

Educational Institutions

- Atlantic Provinces Special Education Authority

Hospitals

- Nova Scotia Hospital

Lending Organizations and Funds

- Housing Development Fund
- Industrial Expansion Fund
- Nova Scotia Business Development Corporation
- Nova Scotia Farm Loan Board
- Nova Scotia Fisheries and Aquaculture Development Fund
- Nova Scotia Housing Development Corporation

Pension Funds

- Members' Retiring Allowances Act Accounts
- Nova Scotia Teachers' Pension Fund
- Public Service Superannuation Fund

Regulatory Bodies

- Public Accountants Board of Nova Scotia

Other

- Environmental Trust Fund
- Insured Prescription Drug Plan Trust Fund
- Nova Scotia Film Development Corporation
- Nova Scotia Gaming Corporation
- Nova Scotia Innovation Corporation
- Nova Scotia Legal Aid Commission
- Nova Scotia Primary Forest Products Marketing Board
- Nova Scotia Talent Trust
- Public Trustee
- Upper Clements Family Theme Park Limited

Financial Statement Audits Performed by Private Sector Auditors

Art Gallery of Nova Scotia
Atlantic Lottery Corporation
Canada-Nova Scotia Offshore Petroleum Board
Check Inns Limited
Council of Maritime Premiers
Halifax-Dartmouth Bridge Commission
Highway 104 Western Alignment Corporation
Nova Scotia Arts Council
Nova Scotia Credit Union Deposit Insurance Corporation
Nova Scotia Liquor Commission
Nova Scotia Municipal Finance Corporation
Nova Scotia Police Commission
Nova Scotia Power Finance Corporation
Nova Scotia Resources Limited
Nova Scotia Utility and Review Board
Public Archives of Nova Scotia
Queen Elizabeth II Health Sciences Centre
Sherbrooke Restoration Commission
Sydney Steel Corporation
Sydney Tar Ponds Cleanup Incorporated
Trade Centre Limited
Waterfront Development Corporation Limited
Workers' Compensation Board of Nova Scotia

Appendix III

PROVINCIAL FINANCE ACT

SECTION 65

Audit and accountants

(1) The Governor in Council shall annually cause the accounts of the Province to be examined and audited by a chartered accountant or accountants, appointed annually for that purpose by the Governor in Council, and may pay the accountant or accountants such salary or remuneration as the Governor in Council determines.

Access to information

(2) Such accountant or accountants shall have access at all times to all sources of information under the control of any department, officer or person expending or collecting public money.

Report of auditors and tabling of report

(3) The accountant or accountants so appointed shall report in writing to the Minister respecting such examination and audit and the Minister shall cause such report to be presented to the House of Assembly during the session next after such examination and audit.

SECTION 65A

The Auditor General shall annually review the estimates of revenue used in the preparation of the annual Budget Address of the Minister to the House of Assembly and provide the House of Assembly with an opinion on the reasonableness of the revenue estimates.