

# Other Audit Observations

# 11 REVIEW OF FINANCIAL STATEMENTS AND MANAGEMENT LETTERS

## INTRODUCTION

- 11.1** The financial statements of crown corporations, agencies and funds of the government of Nova Scotia, and trusts administered by the government of Nova Scotia, are in some cases audited by the Office of the Auditor General and in other cases by private sector auditors licensed under the Public Accountants Act.
- 11.2** Section 17 of the Auditor General Act permits this Office to conduct additional reviews of those entities where financial statements are reported on by private sector auditors. This Chapter of our Report contains comments on our review of the results of financial statement audits by private sector auditors, as well as comments on audits performed by this Office.
- 11.3** The financial statements of the Public Archives of Nova Scotia were subject to a review, rather than an audit, as the operating budget of the Archives is now part of the annual budget of the Department of Tourism, Culture and Heritage.

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## FINANCIAL STATEMENT AUDITS BY PRIVATE SECTOR AUDITORS

- 11.4** We reviewed the audited financial statements and reports prepared by private sector auditors. Our review focused on whether:
- there were any qualifications of auditors' opinions on the financial statements;
  - the audit opinion was based on Canadian generally accepted accounting principles, or on a disclosed basis of accounting;
  - there was any indication of inadequate controls over accounting records; and
  - there was timely preparation and audit of annual financial statements.
- 11.5** The following observations resulted from our review.

### Reservations of Opinion

- 11.6** The auditor of AgriTECH Park Inc. issued a qualified audit opinion on the March 31, 2004 financial statements. The auditor was appointed in the current year and was not able to verify the opening balances which were unaudited, and enter into the determination of the results of operations and cash flows.
- 11.7** The auditor of the Art Gallery of Nova Scotia issued a qualified audit opinion on the March 31, 2004 financial statements. As a charitable organization, the

Art Gallery of Nova Scotia derives revenues from donations, special events, corporate campaigns and other sources. The completeness of this revenue is not susceptible to conclusive audit verification. This is the usual situation for charitable organizations that receive donations.

- 11.8** The auditor of the Nova Scotia E911 Cost Recovery Fund issued a qualified audit opinion on the financial statements. The Fund is managed by the Emergency Measures Organization which has the ability to incur expenses on behalf of the Fund. The completeness of the expenses that the Fund incurs is not susceptible to conclusive audit verification.

### Disclosed Basis of Accounting

- 11.9** As the result of recent changes to the Canadian Institute of Chartered Accountants Handbook, auditors can no longer give unqualified opinions on general purpose financial statements unless the statements comply with Canadian generally accepted accounting principles. The audit reporting on financial statements prepared using a disclosed basis of accounting which is not generally accepted is deemed to be for specific users - not for general purpose - and should include wording similar to the following:

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

This approach to the preparation of financial statements reduces the value of the statements to the House and the general public.

- 11.10** The following entities' financial statements were prepared on a disclosed basis of accounting rather than Canadian generally accepted accounting principles.
- The financial statements for all school boards were prepared using accounting principles for Nova Scotia School Boards as prescribed by the *District School Board Financial Handbook* published by the Department of Education.
  - The Nova Scotia Power Finance Corporation and Sydney Environmental Resources Limited financial statements were prepared on a disclosed basis of accounting.
  - The Sherbrooke Restoration Commission's financial statements were prepared using accounting principles for museum boards in Nova Scotia as prescribed by the Department of Tourism, Culture and Heritage.

### Financial Controls and Records

- 11.11** In certain instances, private sector auditors reported weaknesses in internal control in management letters to crown corporations or agencies. For audits where

management letters were issued, summary observations of the more significant matters included are as follows.

- The auditors of the Tri-District Health Authority (District Health Authorities 1, 2 and 3) noted that the timeline for conversion of the payroll system to SAP may pose an interim risk for payroll support before the conversion can take place.
- The auditors of the Capital District Health Authority (District Health Authority 9) noted various computer-related issues surrounding the change management process, access controls and passwords.
- The auditors of the Colchester East Hants Health Authority (District Health Authority 4) recommended improvements to enable better management and record keeping of capital assets. They noted instances where the Authority's information technology policies could be improved. The auditors also raised concerns over the centralized general ledger shared with two other health authorities related to the lack of access controls and process inefficiencies.
- The auditors of the Cumberland Health Authority (District Health Authority 5) found weaknesses in accounts receivable monitoring and inadequate segregation of duties due to the lack of access controls over the centralized general ledger.
- The auditors of the Guysborough Antigonish Strait Health Authority (District Health Authority 7) commented on the lack of accountability over management of the pharmacy inventory.
- The auditors of the Pictou County Health Authority (District Health Authority 6) noted weaknesses in completion of regular monthly accounting procedures and tracking capital assets. They noted instances where the Authority's information technology policies could be improved. The auditors also raised concerns over the centralized general ledger shared with two other health authorities related to the lack of access controls and process inefficiencies.
- The auditors of the Conseil scolaire acadien provincial, Southwest Regional School Board, Strait Regional School Board and Metropolitan Housing Authority, respectively, suggested that the entities request government to have an independent auditor report on the design and ongoing effectiveness of the internal controls of SAP.
- The auditors of Highway 104 Western Alignment Corporation commented on the design limitations of the tolling system that do not support individual user profiles and passwords for staff.
- The auditors of the Insured Prescription Drug Plan Trust Fund noted several instances where controls over assets or efficiency of the accounting system could be improved.

- The auditors of the IWK Health Centre reiterated prior year's concerns surrounding various computer and access control issues.
- The auditors of the Nova Scotia Health Research Foundation suggested a reconciliation of the grants payable spreadsheet to the accounting records be completed on a regular basis.
- The auditors of Resource Recovery Fund Board Inc. noted that documentation in approved program funding files could be improved. They also reported that the Board's information technology policies and practices could be improved.
- The auditors of the Tri-County Housing Authority raised concerns about the controls over the initiating, processing and payment of expenditures. They also noted that balance sheet accounts are not being reconciled on a regular basis and support for some payroll entries is not retained in the files.
- The auditors of the Waterfront Development Corporation noted that recommended changes to access and password controls identified in prior years had still not been made. They also recommended that the Corporation develop a process to assess whether real estate and development projects are recoverable and whether the carrying amount in the accounting records is appropriate and supportable.

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## **FINANCIAL STATEMENT AUDITS BY THE OFFICE OF THE AUDITOR GENERAL**

- 11.12** The Auditor General is responsible for the annual audit of the consolidated financial statements of the Province of Nova Scotia. See Chapter 2 of this Report for comments and observations on our audit of the Province's March 31, 2004 statements.
- 11.13** The Auditor General is also responsible for the annual financial statement audits of certain crown corporations, agencies, funds and trusts. The following observations resulted from such audits conducted by or for the Office. For the year ended March 31, 2004, the Office contracted nine financial statement audits with private sector audit firms. The Office signed contracts with these firms and provided oversight supervision for the audits. The auditor's report for each set of financial statements was signed by the Auditor General of Nova Scotia.

### **Reservations of Opinion**

- 11.14** The result of an audit is an opinion on whether financial statements present fairly the financial position of the entity at its fiscal year end and the results of its operations for the year then ended. Where there are qualifications of an audit opinion or situations in which it was not possible to render an opinion, we believe it is appropriate to report on such matters.

- 11.15** The auditor's report on the March 31, 2004 financial statements of the Atlantic Provinces Special Education Authority was qualified because the Authority derives revenue from donations and bequests. The completeness of this revenue is not susceptible to conclusive audit verification. This is in common with many organizations that receive donations and bequests. The report was further qualified because the treatment of internally restricted donations and investment income did not comply with Canadian generally accepted accounting principles and certain employee retirement benefits are not accrued and recorded.
- 11.16** The auditor's report on the March 31, 2004 financial statements of the Industrial Expansion Fund referred to a disclosed basis of accounting, as in previous years. An unqualified audit opinion on such general purpose financial statements requires the use of Canadian generally accepted accounting principles. The auditor's report was qualified because certain expenses and revenues were not reflected in the financial statements. As well, a statement of cash flow was not provided and classification and disclosure of receivables was not adequate. The audit matters noted will have to be addressed by the Fund to avoid qualifications in future years.
- 11.17** The auditor's report on the March 31, 2004 financial statements of the Nova Scotia Farm Loan Board was qualified because satisfactory evidence to support management's estimate of the allowance for loan impairment was not provided.
- 11.18** The auditor's report on the March 31, 2004 financial statements of the Nova Scotia Housing Development Corporation was qualified because revenues and expenses related to certain programs under federal-Provincial agreements have not been included in the financial statements.
- 11.19** The auditor's report on the March 31, 2004 financial statements of the Nova Scotia Talent Trust was qualified because the Trust derives revenues from fund-raising activities and donations. The completeness of this revenue is not susceptible to conclusive audit verification. This is the usual situation for this type of organization.
- 11.20** The auditor's report on the March 31, 2004 financial statements of the Public Trustee Trust Funds was qualified because the nature of the Public Trustee's operations makes it impossible to provide an opinion on the completeness of its trust assets. This is not an unusual situation for such trust funds.

## System Weaknesses

- 11.21** During the Office's financial statement audits, situations were noted where accounting and control systems or procedures were deficient. Although they were not of a magnitude to require reservation of an audit opinion, a number of these situations are summarized in this Chapter.
- 11.22** [Nova Scotia Farm Loan Board](#) - There are weaknesses related to the monitoring of loans and a lack of documentation to support the loan valuation process. A

thorough analysis should also be performed to support any changes made to the general allowance for loan impairment.

- 11.23** [Nova Scotia Innovation Corporation](#) - The issue of whether the Corporation has the legislative authority to approve asset write-offs independent of the Province's (i.e., Executive Council) approval should be further investigated by management.
- 11.24** [Nova Scotia Public Service Superannuation Fund](#) - Certain commuted value payments to individuals who left employment with the government, estimated at \$9.8 million, were underpaid since 1992. Management should complete its analysis of the underpayments and implement procedures to ensure amounts are paid out appropriately, on a timely basis. Other issues identified, such as membership data accuracy and user access, relate to the entire pension administration system. This system comprises all pension recipients, including those of the Teachers' Pension Plan and the Sydney Steel Corporation Superannuation Fund. As noted in Chapter 3 (page 17) of this Report, an audit of the pension administration system is in process which may address some of these issues.
- 11.25** [Nova Scotia Public Trustee](#) - The Trustee should move from the cash basis to the accrual basis of accounting in order to comply with Canadian generally accepted accounting principles. As noted in prior years, a reconciliation of the mail book to the deposit slips is needed.
- 11.26** [Nova Scotia Talent Trust](#) - A number of cheques were prepared with only one signature rather than two signatures as required. The Trust should also have appropriate controls on its gala ticket sales to reduce the likelihood of accounting inconsistencies.
- 11.27** [Sydney Steel Corporation Superannuation Fund](#) - There should be an oversight board established to monitor the performance and management of the fund.

### **Timeliness of Financial Reporting**

- 11.28** The Provincial Finance Act requires that financial statements for government business enterprises and governmental units be submitted to the Minister of Finance by June 30 following the fiscal year end (usually March 31).
- 11.29** There was considerable improvement this year in the number of entities that met the submission deadline. There were eight entities (20 in 2003) that were not fully successful in providing audited financial statements and requested information by June 30.
- 11.30** The Province's March 31, 2004 consolidated financial statements were released on September 30, 2004 meeting the new reporting requirement set out in the Provincial Finance Act. The release was six weeks earlier than in the previous year.