Confidential **September 7, 2017**

2016-17 PUBLIC ACCOUNTS

Issue: What is reported in the 2016-17 Public Accounts released on September 7, 2017?

KEY MESSAGES PUBLIC ACCOUNTS:

- The Public Accounts for Ontario show Ontario's deficit for 2016-17 is $991 million. This result is a lower deficit by $3.3 billion than projected in the 2016 Budget, and $0.5 billion lower than the Interim forecast in the 2017 Budget.

- This marks the eighth year in a row that Ontario has beaten its deficit target.

- Ontario has balanced its 2017-18 budget while continuing to invest in the programs and services that matter to Ontarians such as health care, education and infrastructure.

- To help Ontarians better understand their government's finances, new digital tools have been developed that present the Public Accounts data in innovative, visual formats. These tools make Ontario's finances easier to understand, access, and use, and are part of Ontario's commitment to Open Government.

- The government will continue to build on its track record of responsible fiscal management.

- We will continue to move forward and present the Province's finances fairly and accurately. We are on track to balance the Budget by 2017-18, and remain balanced in 2018-19.

KEY MESSAGES: ACCOUNTING CHANGES

BPS REVENUE PRESENTATION

- 2016-17 Public Accounts are presenting third-party revenues for hospitals, school boards and colleges with provincial revenue

- In prior years, these revenues were netted against the expenses of the respective sectors (health, education, post-secondary)

  - This is a change in presentation only; the change increases total revenues and expenses by approximately $8 billion, and does not impact the deficit, net debt or accumulated deficit

- This change is consistent with public sector accounting standards and the reporting practices of other senior Canadian governments

- The Auditor General is supportive of this change in presentation.

ACCOUNTING FOR ENERGY GBEs

- The 2016-17 Public Accounts include the financial results of Ontario Power Generation (OPG) and Hydro One using International Financial Reporting Standards (IFRS)

- These two government business enterprises currently report their stand-alone financial results using Generally Accepted Accounting Principles in the United States (US GAAP).

- In prior years, the reported results of OPG and Hydro One were included in the results of the Province based on US GAAP

- This change does not have a material impact on this year's Public Accounts

- The Auditor General is supportive of this change in presentation.

PENSION ACCOUNTING:

- Further to the 2015-16 Public Accounts, the government established the Pension Asset Expert Advisory Panel to deliver independent advice on how public sector accounting standards are interpreted as they apply to current net pension assets.
- The Pension Asset Expert Advisory Panel has released its independent advice and recommendations on the application of public sector accounting standards for two of Ontario's jointly sponsored pension plans (Ontario Teachers' Pension Plan and the Ontario Public Sector Employees' Union Pension Plan).
- The Panel's report concluded that the Province's share of the net pension assets of both the OTPP and the OPSEUPP should be recognized in Ontario's financial statements.
- The government accepted the Panel's recommendations, which have been reflected in the 2016-17 financial statements.
- The 2015-16 financial statements have also been restated to reflect the pension assets for these two plans.
- In opining on the 2016-17 Public Accounts, the Auditor General continues to not accept the application of the Public Sector Accounting Board (PSAB) standards regarding pension accounting for the Province's jointly sponsored pension plans as interpreted by the Province's accounting professionals and confirmed by the Pension Asset Expert Advisory Panel.
- For 2016-17, the Auditor General has qualified her opinion, stating that the province's deficit is understated by $1.4 billion.

KEY MESSAGE: IESO ACCOUNTING:

- The Independent Electricity System Operator (IESO) reports its financial results in accordance with Public Sector Accounting Standards.
- In 2016 IESO changed its accounting policy to begin recognizing of market assets (amounts due from

power distributors) and liabilities (amounts due to power generators). In previous years, these amounts were omitted from their IESO's financial statements

- As a counterparty to the settlement between power distributors and power generators, it was deemed appropriate that these amounts be reflected to better reflect the impact of the IESO-administered market at year-end.

- In addition, IESO also adopted rate regulated accounting for deferred charges, such as the cost of smart meters, which will be recovered from users of these meters over time.

- Public Sector Accounting Standards are silent on rate-regulated accounting, and as a result, as provided for in the accounting standards, IESO considered other sources of guidance to assess the appropriateness of applying rate regulated accounting.

- Prior to the 2015 merger with the IESO, the Ontario Power Authority (OPA) reported market accounts and used rate-regulated accounting under PSAS. The statements of the OPA were not qualified during that time by OPA's external auditor or the Auditor General. This accounting treatment is not new to Ontario.

- The Auditor General qualified her opinion in 2016-17 based on the recognition of the IESO's market accounts. The Auditor General also noted in her opinion that the use of rate regulated accounting under PSAS is not permitted, but did not qualify on the issue of rate regulated accounting, as the impact was not material in the current year.

- The reporting changes implemented by the IESO were approved by their management and board, and received an unqualified audit opinion from their external auditor. The province's Office of the Provincial Controller also supports the changes.

BACKGROUND:

Pension Expert Advisory Panel

- On November 10, 2016 Ontario established the Pension Asset Expert Advisory Panel to provide advice and recommendations to the government on the application of public sector accounting standards to Ontario's net pension assets.

- The panel was comprised of accounting, legal, and pension experts in the areas of jointly sponsored pension plans, actuarial modelling for pension plans and Public Sector Accounting Standards.

- The following four members appointed to the Panel were:

  - Tricia O'Malley (Chair)
  - Murray Gold
  - Uros Karadzic
  - Paul Martin

- Panel members also provided advice on how to value net pension assets reported on the province's books, taking into account future decisions which might be made by the plan's sponsor or sponsors.

- The Panel issued its report in February 2017. Upon receiving the report, the Government, supported by its own research and analysis, accepted the Panel's recommendation and has reported the pension assets of the Ontario Teachers' Pension Plan (OTPP) and Ontario Public Service Employees' Union Pension Plan (OPSEUPP) in its 2016-17 consolidated financial statements (with restatement of 2015-16).

- The Panel issued a supplementary report in March 2017 with respect to the Healthcare of Ontario Pension Plan (HOOPP) and Colleges of Applied Arts and Technology Pension Plan (CAATPP) recommending that a full valuation allowance be recorded on the net assets of both of these plans, based on the difference in governance structure between these plans and OTPP and OPSEUPP. The Province has recorded a valuation allowance for CAATPP in the year (amount is not material) and the HOOPP plan is not in a net asset position for accounting purposes at March 31, 2017.

Independent Electricity System Operator

- Independent Electricity System Operator (IESO) is a not-for-profit, non-taxable corporation established pursuant to Part II of the *Electricity Act, 1998*. The Ontario Power Authority and the IESO merged January 1, 2015.

- One of IESO's roles is to settle the market accounts, which are the amounts due to the entities who provide electricity to the market (e.g. power generators) and due from those who consume electricity (e.g. local distribution companies on behalf of their consumers).

- Rate regulated accounting is appropriate where the rates an entity is able to charge to its customers are set by another party (i.e. a regulator), provided specified criteria are met. Rate-regulated accounting permits the entity to defer costs that would otherwise be expensed to the period that the related revenue is charged to customers. Costs able to be deferred by the IESO include:
  - Unrecovered smart metering expenses
  - Unrecovered pension and post-employment benefits related to PSAB transition

- During 2016, IESO made two accounting changes (1) to recognize the market accounts in its financial statements – these amounts has not previously been recognized in the IESO's financial statements and (2) to apply rate-regulated accounting.

- The IESO received an unqualified audit opinion from KPMG (their external auditor) with respect to the financial statement presentation in their 2016 audited financial statements. IESO management, IESO's Audit Committee, IESO's Board of Directors, IESO's external auditor, and the Office of the Provincial Controller all support the recognition of the market accounts and the use of rate-regulated accounting by IESO

Revenue Highlights

Against the Restated 2016 Budget:

- Revenues for 2016-17 came in at $140.7 billion, or 2.2 billion higher than forecast in the 2016 Budget. This was largely due to higher than projected taxation revenues, non-provincial source revenues from hospitals, school boards and colleges, and income from GBEs, partially offset by lower than projected Government of Canada transfers and other non-tax revenue.

Against the Restated Interim Estimates in the 2017 Budget:

- Revenues for 2016-17 came in at $140.7 billion, or 0.6 billion lower than interim forecast in the 2017 Budget. This was largely due to lower than projected taxation revenues and Government of Canada transfers, partially offset by higher than projected income from GBEs.

Expense Highlights

Against the Restated 2016 Budget plan:

- Total expense in 2016-17 was $141.7 billion, or 0.1 billion lower than forecast in the 2016 Budget plan. Program spending was $130.0 billion, up by $0.6 billion from a planned spending of $129.4 billion and interest on debt was $11.7 billion, lower by $0.7 billion from planned interest cost of $12.4 billion. Program spending was higher by $0.6 billion largely due to higher than projected spending in the health, community and social services, justice sector and general government and other.

Against the Restated interim Estimates in the 2017 Budget:

- Total expense in 2016-17 was $141.7 billion or $1.1 billion lower than interim forecast in the 2017 Budget. Program spending was $130.0 billion, $0.9 billion lower than the interim forecast of $130.9 billion in the 2017 Budget. Interest on debt was $11.7 billion, lower by $0.2 billion from planned interest cost of $11.9 billion. Program spending was lower by $0.9 billion largely due to lower than projected spending in the health, education and other programs.

Net Debt

- Net debt as of March 31, 2017, was $301.6 billion which was $6.7 billion lower than forecast in the 2016 Budget. Net debt grew by $6.2 billion during the year, representing a $6.6 billion increase in liabilities that was partially offset by a $0.4 billion increase in financial assets.

Prepared by: Bharat Patel, Office of the Provincial Controller
Date Prepared: August 31, 2017
Reviewed by: Mark Donaldson

Approved by:	**Name:**
ADM, Office of the Provincial Controller	Cindy Veinot
Communications Branch	Emilie Smith

Commented [DM(1]: Is this correct?

Appendix

Preparation and Tabling:

The Public Accounts for each fiscal year are prepared under the direction of the President of Treasury Board, as required by the *Financial Administration Act*.

The Public Accounts of Ontario consist of the Annual Report and 3 supplementary volumes. The Annual Report includes the province's audited consolidated financial statements and a financial statement discussion and analysis section. Supplementary information is contained in three volumes:

Volume 1: Ministry statements for expenses, assets, revenue, detailed debt and other supplementary schedules. It provides a comparison of appropriations with actual spending.

Volume 2: Financial statements of significant provincial corporations, boards, commissions that are part of the government's reporting entity, and other miscellaneous statements.

Volume 3: Detailed schedules of payments made by ministries to vendors and transfer payment recipients.

The *Financial Administration Act* requires the President of Treasury Board to submit the province's Annual Report and consolidated financial statements to the Lieutenant Governor in Council (LGIC) on or before 180 days after fiscal year-end. This year, the deadline is September 27, 2017.

The process for release of the Public Accounts is as follows:

- The Public Accounts are approved by the Lieutenant Governor in Council.
- The LGIC lays the Public Accounts before the Assembly, if the Assembly is in session, and the Public Accounts are then released on the same day.
- If the Assembly is not in session on the day of the release of the Public Accounts the LGIC is required to make the Public Accounts public and the Public Accounts are laid before the Assembly <u>on or before</u> the tenth day of the next session.