

Legislative
Assembly
of Ontario



Assemblée
législative
de l'Ontario

STANDING COMMITTEE ON PUBLIC ACCOUNTS

PUBLIC ACCOUNTS OF THE PROVINCE

(CHAPTER 2, 2017 ANNUAL REPORT OF THE OFFICE OF THE AUDITOR
GENERAL OF ONTARIO)

3rd Session, 41st Parliament
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The Honourable Dave Levac, MPP
Speaker of the Legislative Assembly

Sir,

Your Standing Committee on Public Accounts has the honour to present its Report and commends it to the House.

Ernie Hardeman, MPP
Chair of the Committee

Queen's Park
May 2018

STANDING COMMITTEE ON PUBLIC ACCOUNTS

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3rd Session, 41st Parliament

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INTRODUCTION

On February 28, 2018, the Standing Committee on Public Accounts held public hearings on the audit (Chapter 2, 2017 *Annual Report* of the Auditor General of Ontario) of the Public Accounts of the Province administered by the Ministry of Finance and the Treasury Board Secretariat.

The Committee endorses the Auditor's findings and recommendations, and presents its own findings, views, and recommendations in this report. The Committee requests that the Ministry provide the Clerk of the Committee with written responses to the recommendations within 120 calendar days of the tabling of this report with the Speaker of the Legislative Assembly, unless otherwise specified.

ACKNOWLEDGEMENTS

The Committee extends its appreciation to officials from the Treasury Board Secretariat, the Ministry of Finance, the Ministry of Energy, and the Cabinet Office. The Committee also acknowledges the assistance provided during the hearings and report-writing deliberations by the Office of the Auditor General, the Clerk of the Committee, and staff in the Legislative Research Service.

BACKGROUND

Ontario's Public Accounts for the fiscal year ending March 31, 2017, were prepared under the direction of the Minister of Finance (as required by the *Financial Administration Act*) and the President of the Treasury Board. The Public Accounts consist of the Province's annual report, including the consolidated financial statements, and three supplementary volumes of additional financial information.

The government is responsible for preparing the consolidated financial statements and ensuring that this information, including many amounts based on estimates and judgment, is presented fairly. The government is also responsible for ensuring that an effective system of control, with supporting procedures, is in place to authorize transactions, safeguard assets, and maintain proper records.

AUDIT OBJECTIVES AND SCOPE

As required under the *Auditor General Act*, the Office of the Auditor General of Ontario, as the legislature's Auditor, audits the consolidated financial statements, with the objective of providing reasonable assurance that the statements are free of significant errors or omissions and are fairly presented in accordance with appropriate generally accepted accounting principles. The consolidated financial statements, along with the independent Auditor's Report, are included in the Province's annual report.

In 2017, for the second consecutive year, the Auditor General issued a qualified opinion on the Province's consolidated financial statements.

MAIN POINTS OF AUDIT

The Auditor General stated that the consolidated financial statements for 2016/17 are fairly presented with two exceptions:

- The government overstated the net pension assets relating to the Ontario Teachers' Pension Plan (OTPP) and the Ontario Public Service Employees' Union Pension Plan (OPSEUPP). As a result, the Province's net debt and accumulated deficit at March 31, 2017, is understated by \$12.429 billion and the 2016/17 annual deficit is understated by \$1.444 billion. (Net debt is the difference between the government's total liabilities and its financial assets.)
- The government inappropriately recognized and consolidated market account assets and liabilities relating to transactions between power generators and distributors managed by the Independent Electricity System Operator (IESO). As a result, IESO's Other Assets and Other Liabilities at March 31, 2017, are overstated by \$1.652 billion.

The Auditor General stated that the Province's accounting treatments in these two cases did not conform to Canadian Public Sector Accounting Standards (PSAS).

The Auditor's report expressed concern that the proposed accounting treatment for the Fair Hydro Plan could have a material impact on the Province's annual financial results for the year ended March 31, 2018, and could become a significant concern to the Auditor's Office.

The Auditor General continues to express concern regarding the Province's growing debt burden. The Auditor's report stated that after adjusting for the net pension assets of the OTPP and the OPSEUPP and the expected costs of the Fair Hydro Plan, the Province will continue to incur annual deficits, and net debt will continue to increase as the government borrows to finance its operations.

The audit expressed concern that the Province's March 31, 2017, consolidated financial statements recognize rate-regulated assets, which the audit stated is not permitted when applying PSAS to government financial statements. The audit noted that this view is supported by many public-sector accounting experts in Canada, including Auditors General across Canada. (Rate-regulated accounting was developed to recognize the unique nature of entities, such as electric utilities, whose rates are regulated by an independent regulator.) The audit concluded that this did not cause a material misstatement in the 2016/17 consolidated financial statements but stressed that it could do so in the future.

The Auditor General also noted that the government had not shared, on a timely basis, the work performed by external advisors in developing an accounting/financial design for the Fair Hydro Plan, and that delays were experienced in receiving communication from the component auditor of the IESO. The Auditor General recommended the government communicate if and when it would file a regulation that would enable the Auditor General to review the pre-election report. The Auditor encouraged the Ministry of Finance and

Treasury Board Secretariat to ensure that her Office has sufficient time to review and comment on the pre-election report.

O. Reg. 41/18, made in February 2018, stipulates that the deadline for the release of the pre-election report is seven days after the day on which the Minister of Finance moves the Budget motion in 2018.

ISSUES RAISED IN THE AUDIT AND BEFORE THE COMMITTEE

A number of issues were raised in the audit and before the Committee. The Committee considers the issues below to be of particular importance.

The Treasury Board Secretariat (TBS) stated the Province's consolidated financial statements are prepared in accordance with Canadian Public Sector Accounting Standards (PSAS). Treasury Board representatives told the Committee that public sector accounting standards are principle-based and not a prescriptive set of rules. Further, the Committee heard that the PSAS require the application of professional judgement. The Treasury Board said it works closely with the Office of the Auditor General on public accounts.

The Treasury Board said it made several accounting changes in 2016/17, including accounting for market accounts and adopting the rate-regulated accounting used by the Independent Electricity System Operator (IESO), and reporting pension assets for jointly sponsored pension plans. The Treasury Board stated that if professional accountants in the public service do not agree with the Auditor General, it is "not as simple as agreeing to accept the Auditor General's interpretation."

The Committee asked if the Treasury Board, Ministries, or the IESO sought the Auditor General's advice prior to drafting the legislation for the Fair Hydro Plan. The Treasury Board and the IESO responded that the Auditor's feedback was sought after the policy decision was made. The Treasury Board indicated that it equipped itself to execute the government's preferred policy direction to the best of its abilities. The audit noted the government did not inform the Auditor's Office of its engagements with external advisors until after the Office became aware that significant discussions were being held on matters related to the Fair Hydro Plan.

The Committee asked if the Treasury Board and the Ministries' staff gave the Ministries and the Premier their best impartial advice regarding the Fair Hydro Plan and rate-regulated accounting. The Committee was told that it is the role of the public service to provide the best objective advice to the elected government and to comply with codes of professional conduct. The Ministry of Energy stated that their advice was given in accordance with the government's policy direction to provide rate relief for Ontario consumers by shifting the costs of social programs from the rate base to the tax base.

The Committee asked why the IESO made the decision to include market assets in 2017 and not five years earlier. The IESO said it had previously considered making the change to rate-regulated accounting when the Ontario Power Authority (OPA) and the IESO merged. The Committee asked if the Ministry of Energy directed the IESO to start using rate-regulated accounting. The IESO

responded that it was its own decision to adopt rate-regulated accounting. The Controller for the Province of Ontario noted earlier that she asked the IESO to consider whether or not rate-regulated accounting was appropriate accounting treatment when she first learnt that the IESO had a second set of market accounts that were not reflected in the IESO's financial statements. The President and CEO of the IESO stated that rate-regulated accounting has the added advantage of giving better visibility to the \$17 billion from market activity that happens on an annual basis, and is in line with six of eight independent system operators across North America that also use rate-regulated accounting.

The IESO told the Committee that its financial statements are the purview and ownership of the management of the IESO, and that the IESO's policies are agreed to by their external advisors, KPMG. The Committee questioned if the IESO can have sole ownership and purview of its financial statements if it is a subordinate body to the Legislature. The Committee then asked if the Province's agencies, boards, commissions and crown corporations are independent from the Auditor General's considerations. The Ministry of Finance responded that these entities have their own governance and their own boards from which they need approval.

The IESO also indicated that PSAS neither explicitly permit nor prohibit the recognition, measurement, presentation, or disclosure of rate-regulated activities. The Auditor's report stated that "the silence of Canadian PSAS on rate-regulated accounting means that rate-regulated accounting is not permitted." As noted earlier, the Auditor's report added, "This view is and has been supported by many public-sector accounting experts in Canada including Auditors General across Canada, private accounting firms, and others, such as the recently retired Director of the Public Sector Accounting Standards Board, who have extensive experience in developing and applying Canadian PSAS."

The Committee pressed the IESO if it could follow the Auditor General's second recommendation to remove Market Accounts. The IESO noted there is a "disagreement" between the IESO and Auditor General on which type of accounting treatment is most appropriate for the IESO. The IESO stated that rate-regulated accounting is the most appropriate way of representing its financials. The audit noted that the Market Accounts do not meet the criteria for recognition as assets and liabilities in the Province's consolidated financial statements.

CONSOLIDATED LIST OF COMMITTEE RECOMMENDATIONS

The Standing Committee on Public Accounts recommends that:

- 1. Government accounting practices, and those of its agencies, that affect the consolidated financial statements of the Province, must be carried out in accordance with Canadian Public Sector Accounting Standards.**
- 2. The Office of the Controller for the Province of Ontario should provide copies of all terms of reference to the Auditor General's Office when they engage private sector firms for accounting advice or opinions.**

**APPENDIX – DISSENTING OPINION OF THE MEMBERS OF THE
PROGRESSIVE CONSERVATIVE PARTY**

Dissenting Opinion of the Members of the Progressive Conservative Party.

The inclusion of a dissenting opinion in a majority report at Public Accounts Committee is a rare occurrence, and is normally only pursued as a symptomatic response to a failure of one or more parties to abide by the generally accepted principles that guide the committee to work effectively and in a non-partisan fashion.

The first of these principles is a clear understanding of the Auditor General's role, and a deference to the impartiality of their office. A core tenant of the Public Accounts Committee is that its members recognize that the opinions and recommendations put forward by the Auditor General are independent and reputable. Proper consideration is meant to be given in response to the Auditor General's findings, and any conflicting conclusions by the committee need to concretely justified and discussed openly.

The second principle is one of constraining partisanship, a concept where in members of the committee are strong and secure in their ability to be non-partisan, and able to collaboratively construct solutions and recommendations.

If one or both of these principles is not respected, than the integrity of the committee, and its reports, come in to question.

In the case of this report, the committee has not addressed the Auditor General's concerns in a manner that could be at all considered effective, particularly in regard to the issues arising from the Government's use of external advisors and accounting firms when developing accounting and financial structures and positions. Concern was raised in the Auditor's report on how the activities of these external advisors were not brought to the attention of their office until that information was specifically requested. These issues were identified as being related to other significant concerns in the report, including with those involving the IESO and the inappropriate accounting of market account assets and liabilities.

Recommendations that should have been approved for inclusion in the final report to address these issues, but are not, include:

- Requiring that all subordinate entities of the legislature whose financial statements impact the consolidated financial statement require approval from the Auditor General on the appointment of their auditor;
- Requiring that any subordinate body of the legislature that employs the same firm to both provide accounting advice and to be their auditor, seek approval to do so from the Auditor General, and;
- That the Office of the Controller for the Province of Ontario should provide copies of all terms of reference to the Auditor General's office when other ministries or government agencies engage private sector firms for accounting advice or opinions.

The implementation of effective recommendations such as these was frustrated by the government's lack of motivation or interest to engage in thoughtful discussion on these issues, which is contrary to the principles and objectives of the committee.

As such no other option was left but to officially state on the record, through a dissenting report, that due to partisanship throughout the committee process this report does not fulfil its responsibility to provide effective and non-partisan recommendations to the government.