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Qs & As

Auditor General's Response to the 2018 Pre-Election Report

Updated: April 23, 2018

Key Messages

- The province is committed to providing high-quality financial reports that support transparency and accountability in reporting to the public and the legislature.
- The purpose of the 2018 Pre-Election Report on Ontario's Finances is to outline the province's estimated revenues and expenses and other details of the fiscal plan before the start of the provincial election.
- We appreciate the work of the Auditor General in ensuring the public receives an independent assessment of the province's finances in advance of the next general election.
- We are pleased with the Auditor General's determination that the majority of the province's estimates regarding revenue, program expenses and interest on debt are based on prudent and cautious assumptions, as required by the Fiscal Transparency and Accountability Act.
- Ontario's fiscal policy is based on cautious assumptions and recognizes the need for flexibility to respond to changing circumstances. During this period of rapid economic change, the fiscal plan considers the impact of today's choices on different groups within the province and on future generations.

Questions and Answers

Reliability of Financial Statements

1. **How can we trust your financial statements when their reliability is repeatedly called into question by independent officers of the legislature?**

- The province has the utmost respect for all independent officers of the legislature, and values the important perspective they bring.
- We are pleased with the Auditor General's determination that the majority of the province's estimates regarding revenue, program expenses and interest on debt are

based on prudent and cautious assumptions, as required by the Fiscal Transparency and Accountability Act.

- Ontario's fiscal policy is based on cautious assumptions and recognizes the need for flexibility to respond to changing circumstances. During this period of rapid economic change, the fiscal plan considers the impact of today's choices on different groups within the province and on future generations.
- We are committed to providing high-quality financial reports that support transparency and accountability in reporting to the public, the legislature, and other users.

2. The Auditor General says that the Pre-Election Report is not a reasonable presentation of the province's finances due to the understatement of deficits from net pension assets and the Fair Hydro Plan. How do you respond?

- We appreciate the work of the Auditor General in ensuring the public receives an independent assessment of the province's finances in advance of the next general election.
- We are pleased with the Auditor General's determination that the majority of the province's estimates regarding revenue, program expenses and interest on debt are based on prudent and cautious assumptions, as required by the Fiscal Transparency and Accountability Act.
- The province is committed to providing high-quality financial reports that support transparency and accountability in reporting to the public and the legislature.
- In developing Ontario's Fair Hydro Plan (OFHP), the government considered a range of implementation options and consulted with legal, accounting, financial and energy sector third-party experts to provide advice and ensure due diligence was completed.
- The impact of the Fair Hydro Plan is transparently disclosed in the December 31, 2017 financial statements of the Independent Electricity System Operator (IESO) and Ontario Power Generation (OPG), which have been released with unqualified (or clean) audit opinions from their external auditors. It will also be transparent in the consolidated financial statements of the province, which will be released in Public Accounts later this year.
- With regards to the matter of net pension assets, PSAS neither requires unilateral control to record an asset, nor does it include a requirement to obtain a letter from the co-sponsor of the plan agreeing to reduce further contributions within 12 months.
- The province will evaluate the need for a valuation allowance annually taking into consideration (a) changes, if any, in the governance structures of the plans, (b), decisions, if any, of the joint sponsors that impact the need for a valuation allowance, and c) changes, if any, in PSAS.
- The province has a strong track record of producing high-quality financial reports on a timely basis, and we will continue to move forward and present the province's finances

fairly and accurately and in accordance with Public Sector Accounting Standards (PSAS).

Province's Fiscal Situation

3. **Do you think that the Pre-Election Report provides an accurate picture of the province's finances?**

- Yes. We are committed to providing high-quality financial reports, like the Pre-Election Report, that support transparency and accountability in reporting to the public, the legislature, and other users.
- The province's financial statements are prepared in accordance with Canadian Public Sector Accounting Standards (PSAS).
- The 2018 Pre-Election Report presents the three fiscal years (2018-19 to 2020-21) covered in the Budget's medium-term fiscal outlook.
- The report includes details of the government's medium-term fiscal plan. The medium-term fiscal plan is based on government policy decisions and direction, as well as estimates built on reasonable assumptions at the time it is developed.

4. **The Auditor General's math shows that there is a hidden deficit on the books – nearly twice as much as the government has said. How can we believe your financial statements?**

- The province continues to move forward and present the province's finances fairly and accurately and in accordance with Public Sector Accounting Standards (PSAS).
- Because the Office of the Auditor General's views differ from the government's with regards to the accounting treatment for net pension assets and the Global Adjustment Refinancing of Ontario's Fair Hydro Plan, there is a difference in the deficit reflected on the province's financial statements.
- The province has the utmost respect for all independent officers of the legislature, and values the important perspective they bring.
- We are pleased with the Auditor General's determination that the majority of the province's estimates regarding revenue, program expenses and interest on debt are based on prudent and cautious assumptions, as required by the Fiscal Transparency and Accountability Act.
- Ontario's fiscal policy is based on cautious assumptions and recognizes the need for flexibility to respond to changing circumstances. During this period of rapid economic change, the fiscal plan considers the impact of today's choices on different groups within the province and on future generations.

- The province has a strong track record of producing high-quality financial reports on a timely basis, and we will continue to move forward and present the province's finances fairly and accurately and in accordance with PSAS.

5. **How can you say that the province includes prudence and flexibility in its fiscal management when just months after announcing a balanced budget, there is a plan to go back into a deficit of $8B?**

- The Fiscal Transparency and Accountability Act, 2004 (FTAA), sets out the governing principles requiring Ontario's fiscal policy to be based on cautious assumptions and to recognize the need for flexibility to respond to changing circumstances.
- The reserve has been set at $0.7 billion in each year between 2018–19 and 2020–21 and over the recovery plan period. This level balances confidence that the economy is performing well while also acknowledging challenges ahead such as trade uncertainty with the United States, rising interest rates and increased household debt.
- Since FTAA was introduced in 2004, the government has never needed the reserve to meet its fiscal targets.
- In addition to the reserve, the current outlook also maintains contingency funds to help mitigate expense risks – particularly in cases where health and safety may be compromised, services to the most vulnerable are jeopardized, or in the event of natural disasters – that may otherwise negatively impact Ontario's fiscal.
- Furthermore, in keeping with sound fiscal practices, the Province's revenue outlook is based on prudent economic assumptions.

6. **Ontario is the most indebted sub-sovereign jurisdiction in the world. Interest on debt payments are increasing by at least five per cent every year – a higher than average growth compared to health and education spending. If you had responsibly managed finances, we could direct this money to programs Ontarians need the most – rather than continuing to go further and further into debt. How can you justify this reckless fiscal management?**

- Since 2014, Ontario's economy has grown more than all G7 countries. Ontario's economy continues to perform well in an increasingly challenging global environment.
- All forecasters expect that Ontario's economy will continue to grow, but at a more modest pace. The government is making strategic investments in programs and services that will generate economic growth.
- As a result, beginning in 2018-19, the province is projecting modest deficits of less than one per cent of GDP.
- While running deficits, Ontario's net debt-to-GDP will remain below its 2014-15 peak of 39.3 per cent and resume a downward trend in 2022-23.

- Ontario's plan to a balanced budget includes important investments in public services and fiscal responsibility.

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7. Why does this government continue to spend at the expense of future generations?

- Ontario's fiscal policy is governed by principles that are based on cautious assumptions and recognize the need for flexibility to respond to changing circumstances. During this period of rapid economic change, the fiscal plan considers the impact of today's choices on different groups within the province and on future generations.
- The government recognizes there are risks to Ontario's economic outlook – an aging population, rising interest rates, and increasing household debt.
- More recently, the potential for changes to NAFTA and other protectionist measures could disrupt trade patterns, and tax reform underway in the United States could lessen Ontario's competitiveness.
- The government's investments will contribute to the growth of the provincial economy.

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8. The government is paying an enormous amount of money just paying the interest on its debt. How are you addressing this?

- Through prudent and cost-effective debt management, the government has consistently kept interest on debt costs below budget projections. Ontario's debt-to-GDP has fallen steadily and will resume a downward trend in 2022-23.
- To minimize interest on debt costs over the long term, the government manages its borrowing program prudently.
- The government's long-term borrowing forecast for 2018-19 is $0.5 billion less than the forecast in the 2017 Budget. Savings from lower-than-forecast interest rates in the 2017 Budget have also offset the additional interest cost from deficits.
- By capitalizing on low interest rates and the strong demand for Ontario bonds in 2017-18, the government has already prefunded $11.5 billion of our 2018-19 borrowing requirement.

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9. The province is already spending massive amounts just on interest on debt – not even paying off principal amounts. What if interest rates rise again?

- To reduce risks and save on interest on debt costs, the government has capitalized on the province's ability to raise funds at low interest rates. Over the last seven years, the government has issued over $70 billion of bonds with terms of longer than 30 years to lock in low rates, and to protect the province from rising interest rates.

- In the year 2000, Ontario was paying about 15.5 cents of every dollar of revenue to service the province's debt. In 2017-18, Ontario is only paying eight cents – the lowest level in 25 years.

- That ratio is predicted to remain in this range over the next three years, even though the interest rate forecast used in the 2018 Budget projections is prudent and assumes rates will rise modestly.

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10. The Financial Accountability Officer has said in the past that your debt reduction commitments are based on unrealistic assumptions. You base a lot of projections on optimistic assumptions about Ontario's growth. Are your projections realistic and sustainable?

- A wide range of assumptions and planning tools help build prudence into Ontario's fiscal plan, including:
  - Estimated revenue, starting with the assumption that economic performance will be slightly lower than expected, as a margin of caution;
  - Contingency funds in each year to help mitigate risks that might otherwise have a negative impact on results; and
  - A reserve in each year to protect against unexpected and adverse changes in the Province's revenue and expense outlook.

- The government has beaten its fiscal targets every year since the recession through prudent and cost-effective debt management. By overachieving on its fiscal targets, the province's net debt is projected to be $36.2 billion lower than it otherwise would have been.

- The Ministry of Finance economic planning assumptions are slightly below the average from private-sector forecasters for Ontario real GDP growth. Three economic experts reviewed the 2018 Budget economic assumptions and found them to be reasonable.

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Personal Income Tax

11. The Auditor General states that you are over-estimating expected revenue from personal income tax. How do you respond?

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Ontario's Fair Hydro Plan Accounting

12. Are you concealing the true cost of Ontario's Fair Hydro Plan? How can we trust this government's financial statements?

- The province's financial statements are prepared in accordance with Public Sector Accounting Standards (PSAS).

- The debt borrowed directly by the province is included in the gross debt of the province in the same way that all other debt issued by the province is recorded.
- The debt issued by either the Fair Hydro Trust of Ontario Power Generation (OPG) is recorded on the consolidated financial statements of OPG. OPG is reflected in the province's consolidated financial statements as an investment, which is the required treatment under PSAS for government business enterprises.
- The method used to record OPG in the consolidated financial statements of the province is the same method that has been used since the Province began recording its investment in OPG 17 years ago.
- The impact of the Fair Hydro Plan is transparently disclosed in the December 31, 2017 financial statements of the Independent Electricity System Operator (IESO) and Ontario Power Generation (OPG), which have been released with unqualified (or clean) audit opinions from their external auditors. It will also be transparent in the consolidated financial statements of the province, which will be released in Public Accounts later this year.

13. Is your accounting structure for the Fair Hydro Plan an example of fraud?

- No. The province's financial statements are prepared in accordance with Public Sector Accounting Standards (PSAS).
- In developing Ontario's Fair Hydro Plan (OFHP), the government considered a range of implementation options and consulted with legal, accounting, financial and energy sector third-party experts to provide advice and ensure due diligence was completed.
- The impact of the Fair Hydro Plan is transparently disclosed in the December 31, 2017 financial statements of the Independent Electricity System Operator (IESO) and Ontario Power Generation (OPG), which have been released with unqualified (or clean) audit opinions from their external auditors. It will also be transparent in the consolidated financial statements of the province, which will be released in Public Accounts later this year.

Pension Asset Accounting

14. Why do you continue to disagree with the Auditor General on the pension asset accounting issue?

- The province continues to move forward and present the province's finances fairly and accurately and in accordance with Canadian Public Sector Accounting Standards (PSAS).
- PSAS neither requires unilateral control to record an asset, nor does it include a requirement to obtain a letter from the co-sponsor of the plan agreeing to reduce further contributions within 12 months.
- The province will evaluate the need for a valuation allowance annually taking into consideration (a) changes, if any, in the governance structures of the plans, (b),

decisions, if any, of the joint sponsors that impact the need for a valuation allowance, and c) changes, if any, in PSAS.

- The province is open to continuing discussions in the hopes of resolving this matter.

Audit Opinions

15. Are you concerned that the Auditor General may issue an adverse opinion on the province's consolidated financial statements, given her reaction to the Pre-Election Report?

- We are pleased with the Auditor General's determination that the majority of the province's estimates regarding revenue, program expenses and interest on debt are based on prudent and cautious assumptions, as required by the Fiscal Transparency and Accountability Act.
- It would be inappropriate to speculate about how the Auditor General may issue an opinion for the 2017-18 Public Accounts.
- The province has a strong track record of producing high-quality financial reports on a timely basis, and we will continue to move forward and present the province's finances fairly and accurately and in accordance with Public Sector Accounting Standards (PSAS).
- The province has the utmost respect for all independent officers of the legislature, and we value the important and necessary perspective they bring. We will continue to work closely with the Office of the Auditor General to identify audit issues early and to ensure that stakeholders are engaged in discussions regarding risks and resolution.

16. Can the Auditor General issue a qualified opinion on the Pre-Election Report?

- The *Fiscal Transparency and Accountability Act* requires the Auditor General of Ontario to review the pre-election report and issue a statement – not an audit opinion – on the results of that review.
- We are pleased with the Auditor General's determination that the majority of the province's estimates regarding revenue, program expenses and interest on debt are based on prudent and cautious assumptions, as required by the Fiscal Transparency and Accountability Act.

17. Other Auditor Generals agree with how the Ontario Auditor General has characterized the issues with the province's finances. How do you respond?

- The province has the utmost respect for all independent officers of the legislature, and we value the important and necessary perspective they bring.

- Public Sector Accounting Standards (PSAS) are principle based – they are not a set of specific prescriptive rules. Applying them requires the application of professional judgment.

- All Chartered Professional Accountants (CPAs), including those employed by the Ontario Public Service (OPS), are required to comply with the Code of Professional Conduct for CPAs. One of those rules is that they not be associated with false or misleading information.

- That means that if the professional accountants in the OPS do not agree with the judgment of the Ontario Auditor General, it is not as simple as agreeing to accept the interpretation of the Office of the Auditor General if they believe that interpretation would result in false or misleading financial statements.

- While we expect professional accountants to agree on the vast majority of issues, we acknowledge that they may not agree on everything and when that occurs, and the difference is material to the financial statements, the Office of the Auditor General can choose to issue a qualified audit opinion.

- The province has a strong track record of producing high-quality financial reports on a timely basis, and we will continue to move forward and present the province's finances fairly and accurately and in accordance with PSAS.

Relationship with the Auditor General

18. Did the government cooperate with the Office of the Auditor General for their review of the Pre-Election Report?

- The province's professional staff works closely and constructively with the Office of the Auditor General on a number of matters, including the Pre-Election Report.

- Staff of Treasury Board Secretariat and the Ministry of Finance proactively worked with the Office of the Auditor General for the past few months to engage in planning and preparatory work for the development and review of a Pre-Election report.

- The province continues to engage all officers of the legislature to engage constructively to ensure the people of Ontario are provided with an independent review of the Province's fiscal position in advance of the election.

19. You say that accountability and transparency are driving forces in pieces like the Pre-Election Report. Would the Auditor General agree with this characterization? Why did you wait so long to announce whether or not you were even going to issue a Pre-Election Report?

- The province is committed to providing high-quality financial reports that support transparency and accountability in reporting to the public and the legislature.

- The province's professional staff works closely and constructively with the Office of the Auditor General on a number of matters, including the Pre-Election Report.

- We look forward to working collaboratively with the Auditor General to ensure the public receives an independent assessment of the province's finances in advance of the start of the next general election.

20. Why do you continue to disagree with the Auditor General?

- The province has the utmost respect for all independent officers of the legislature, and we value the important and necessary perspective they bring.
- Public Sector Accounting Standards (PSAS) are principle based – they are not a set of specific prescriptive rules. Applying them requires the application of professional judgment.
- All Chartered Professional Accountants (CPAs), including those employed by the Ontario Public Service (OPS), are required to comply with the Code of Professional Conduct for CPAs. One of those rules is that they not be associated with false or misleading information.
- That means that if the professional accountants in the OPS do not agree with the judgment of the Ontario Auditor General, it is not as simple as agreeing to accept the interpretation of the Office of the Auditor General if they believe that interpretation would result in false or misleading financial statements.
- While we expect professional accountants to agree on the vast majority of issues, we acknowledge that they may not agree on everything and when that occurs, and the difference is material to the financial statements, the Office of the Auditor General can choose to issue a qualified audit opinion.
- The province has a strong track record of producing high-quality financial reports on a timely basis, and we will continue to move forward and present the province's finances fairly and accurately and in accordance with PSAS.

Contingency Fund

21. Why is the Contingency Fund being increased by $1 billion in 2018-19?

- The government has taken measures to ensure an appropriate level of prudence and flexibility is built into the fiscal plan.
- The fiscal plan includes contingency funds (both operating and capital) to help mitigate expense risks, particularly in cases where health and safety may be compromised or services to the most vulnerable are jeopardized, that may otherwise adversely affect Ontario's fiscal performance.
- From 2008-09 to 2017-18, the total Contingency Fund allocation has ranged from $500 million up to $3.4 billion. As such, the 2018-19 Contingency Fund allocation of $1.6 billion is within its historic range.

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