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Chapter 1

Introductory Comments by the Auditor General

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Introductory Comments by the Auditor General

Volume IV Reports our Financial Audit Work

Province receives clean audit opinion

1.1 This volume of our Report deals with matters arising from our financial audits of the Province and its Crown agencies for the year ended March 31, 2016.

1.2 On September 27, 2016 I signed an unqualified audit opinion on the 2016 consolidated financial statements of the Province of New Brunswick.

Significant change from 2015

1.3 This represents a significant change from the prior year when the Province received its first qualified audit opinion in 17 years. The reservations expressed in the prior year qualified audit opinion related to concerns regarding accounting for the Province's shared risk pension plans.

Province changed its position on the accounting for shared risk pension plans

1.4 In 2016, the Province revised the accounting for its shared risk pension plans. As a result of the Province's accounting change for these pension plans, I was able to issue an opinion without reservations.

Other significant audit and accounting issues also addressed in 2016

1.5 In addition, the Province addressed other significant accounting issues during the 2016 audit such as consolidation of the Province's not-for-profit nursing homes, and the presentation of the contingency reserve in the Province's audited financial statements. The Province also implemented a number of prior year financial statement audit recommendations, including forming an audit committee, which was announced in a September 23, 2016 news release "*Government establishes audit committee*".

1.6 Chapter 3 in this volume contains further details on

accounting for pensions, nursing homes and the contingency reserve. Chapter 4 contains details of other accounting findings from the Province's March 31, 2016 financial statement audit, as well as details of the implementation of prior year audit recommendations.

Pleased with the Province's 2016 progress on accounting and audit issues

1.7 Overall I am very pleased with the progress made this year in resolving the Province's prior year audit and accounting issues. My Office worked collaboratively with the Office of the Comptroller and other senior government officials to address and resolve these issues, and we hope this positive implementation and cooperation trend continues in future years' financial statement audits.

Auditor General's Comments on the Province's Fiscal Status

1.8 The Province's fiscal situation remains a significant concern. The Province's March 31, 2016 financial statements note the Province has its eighth consecutive deficit since 2009. From 2009 to 2016 annual deficits have occurred totaling approximately \$3.5 billion cumulatively, and approximately \$6 billion (or 43%) of the Province's \$14 billion total Net Debt has been added in this period.

Unfavourable long-term sustainability indicators

1.9 Chapter 2 presents our assessment of commonly used indicators of financial condition for the Province. While mostly neutral or favourable results have occurred for the Province's long-term flexibility and vulnerability indicators, unfavourable results have largely occurred for long-term sustainability indicators.

Deficits are planned to continue until 2020-2021

1.10 This pace of accumulating deficits and growth of Net Debt is not sustainable for the Province of New Brunswick's population and resources. Further, the 2016-2017 budget speech announced that deficits are planned to continue until 2020-2021.

Net Debt planned to grow by almost \$1 billion until 2020-2021

1.11 The budget speech indicated from 2016-2017 to 2019-2020 annual deficits will be incurred each year, which will further increase the Province's accumulated deficit and Net Debt at the end of fiscal 2019-2020 by a total of \$830 million. I am very concerned with the government's fiscal plan that continues New Brunswick's Net Debt growth by almost \$1 billion until 2020-2021.

Continued diligence is needed to improve the financial health of the Province

1.12 Continued fiscal diligence is required in government policy and decision making to further improve the financial health of the Province.

Crown agencies and Federal claims audits

1.13 Chapter 5 reports on matters arising from our audits of Crown agencies and Federal claims. In this chapter we highlight recurring themes in our findings on Crown agency audit work.

Concerning continued findings re Crown agency oversight/governance

1.14 Of particular concern are the oversight/governance findings encountered in our Crown agency work which include findings such as lack of regular board meetings, lack of oversight of key decisions, delays in publishing annual reports, lack of risk management or internal control oversight, weaknesses in conflict of interest disclosures and other oversight/governance weaknesses.

New theme in 2016 Crown agency findings re financial management/cash concerns

1.15 Also concerning in 2016 was the emergence of a new theme in the Crown agency findings relating to financial management/cash. We saw such findings in eight of our Crown agency audits. The findings included items such as:

- insufficient management of inventory and lack of proper inventory ordering quantity;
- delays in implementing investment policies;
- lack of approval of budgets used for comparison purposes in the audited financial statements;
- payment of duplicate invoices;
- a violation of the *Financial Administration Act* (in terms of obtaining appropriate spending approvals where budgets are overspent); and
- a lack of proper procedures for safe guarding of cash.

New Brunswick Lotteries and Gaming Corporation audit findings remain very concerning

1.16 As well, the New Brunswick Lotteries and Gaming Corporation (NBLGC) audit findings continue to remain very concerning. The financial audit for this Crown agency is behind. At the time of writing this chapter, the most recent audited financial statement for NBLGC was for the year ended March 31, 2014.

1.17 In addition, the recent joint performance audit by the Atlantic Auditors General found several governance issues and issues in the structure of the Province's arrangements with the Atlantic Lottery Corporation. A different structure should be considered for NBLGC to ensure it is effectively meeting the needs of government and taxpayers.

1.18 In my view, Newfoundland and Labrador's structure where the provincial lotteries operate as a division within the Department of Finance (not as a separate Crown agency) should be reviewed and considered in any determination of NBLGC's future structure. The efficiency and simplicity in such a structure merits a closer look for application in New Brunswick.

Renewal of “mission critical” Systems

1.19 In the course of our financial audit work, we examine certain of the Province's information technology systems. The systems we examine tend to focus on “mission critical” aspects of financial data and information processing such as: payroll processing, payment processing, financial reporting systems etc.

1.20 We made the following observations:

- one system (for teachers and certain school district employee payroll) is outdated and may be at risk of failure;
- two systems (for the Province's public servants' payroll and for the Province's vendor payments) may no longer be fully supported as of 2017;
- there are some redundant systems causing significant inefficiencies in processing financial information; and
- there have been delays in implementing the Province's new ERP (Enterprise Resource Planning) system.

Current IT weaknesses may have significant consequences

- 1.21** These IT weaknesses may have significant consequences such as:
- timely processing of the Province’s payroll may be at risk if action is not taken to address these ongoing issues;
 - these weaknesses could cause a potential impact on service delivery;
 - the availability of financial information for decision making or other purposes may also be at risk; and
 - unnecessary resources are being consumed in operating inefficient systems.

Government should prioritize replacement of aging and at risk IT infrastructure

- 1.22** In my view, government should prioritize replacement of aging and at risk IT infrastructure to ensure “mission critical” systems continue to operate ensuring delivery of essential services to the taxpayers of New Brunswick. Further details on information systems findings are found in Chapters 4 and 5 of this volume.

Acknowledgements

- 1.23** Overall, my Office is grateful for the continuing cooperation we receive from government departments and agencies during the course of our financial audit work.

- 1.24** I want to thank all staff from my Office for their hard work and dedication. It is a small group of professionals committed to fulfilling the mandate of the Office and producing a quality report to the Legislative Assembly. The report we are presenting today is a reflection of a team effort where each member of the staff has greatly contributed.



Kim MacPherson, CPA, CA
Auditor General

Chapter 2

Comments on the Province's Financial Position

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Comments on the Province's Financial Position

Eighth Consecutive Annual Deficit

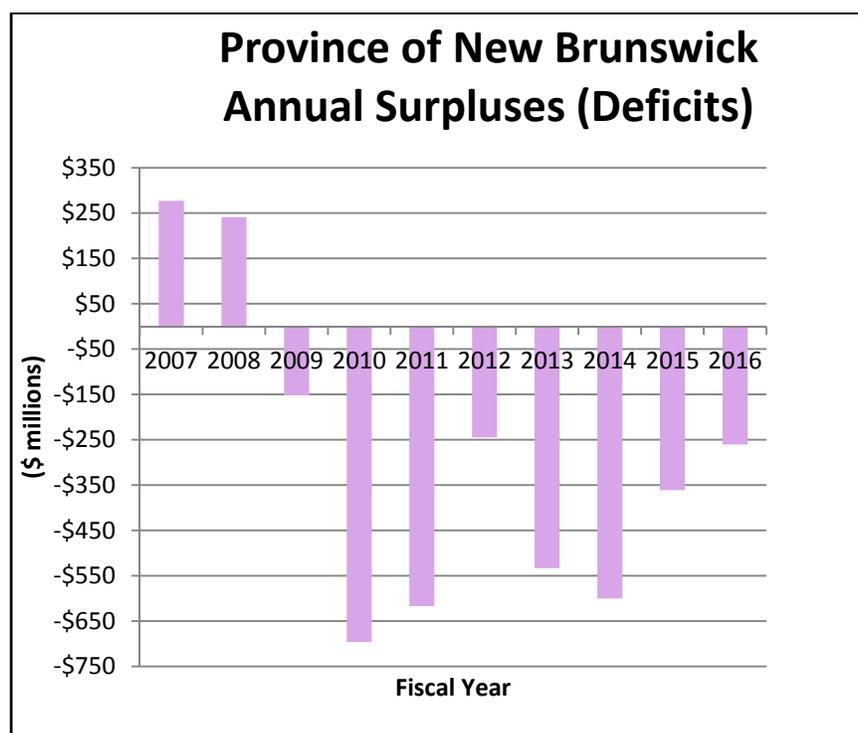
2.1 The Province's March 31, 2016 audited consolidated financial statements reported a deficit of \$260.5 million and an increase in Net Debt for the fiscal year of \$541.4 million. The Province now has a Net Debt of \$13.7 billion.

2.2 The \$260.5 million annual deficit was lower than the budgeted deficit of \$326.8 million and was lower than the prior year deficit of \$361.4 million.

Action is Required

2.3 This represents the eighth consecutive annual deficit. To assist in financing these deficits, the Province has incurred additional debt. This trend is very concerning. Significant changes are required to improve the financial health of the Province.

Exhibit 2.1 - Annual Surpluses (Deficits)



As restated

Exhibit 2.2 - Annual Surpluses (Deficits) Data

Annual Surpluses (Deficits)										
(\$ millions)										
	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
As restated	277.3	241.1	(152.0)	(695.9)	(617.2)	(244.8)	(533.2)	(600.4)	(361.4)	n/a
As originally recorded	236.8	86.7	(192.3)	(737.9)	(633.0)	(260.6)	(507.7)	(498.7)	(388.6)	(260.5)

See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

2.4 Exhibits 2.1 and 2.2 show the surplus or deficit for the past ten years. The preceding years' amounts have been restated as per Note 17 of the Province's March 31, 2016 consolidated financial statements.

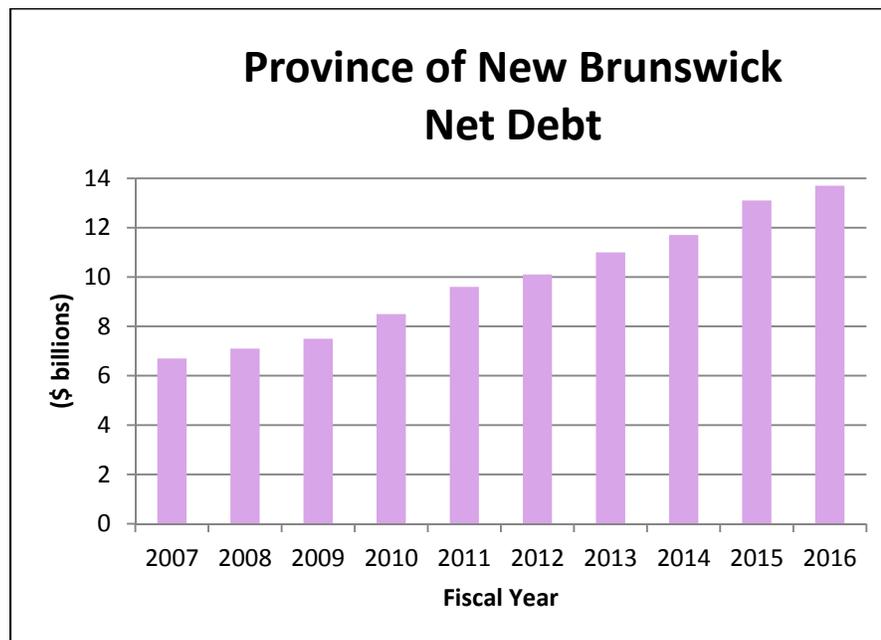
2.5 It is important to note that the years prior to 2015 have not been restated in the exhibits above or in other exhibits in this chapter for the impact of the nursing homes consolidation in 2016 as the information is not available. Significant variances to data presented in this chapter may have occurred for 2014 and earlier years as a result of this

accounting change. Further information on the nursing homes consolidation accounting is contained in Chapter 3.

Continued Growth in Net Debt

2.6 Net Debt is one of the most important measures of the financial position of the Province. Exhibits 2.3 and 2.4 show Net Debt for the past ten years. Net Debt measures the difference between a government's liabilities and financial assets. This difference provides a measurement of the future revenues required to pay for past transactions and events.

Exhibit 2.3 - Province of New Brunswick Net Debt



See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

Exhibit 2.4 - Net Debt Data

Net Debt (\$ billions)										
	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
As restated	6.7	7.1	7.5	8.5	9.6	10.1	11.0	11.7	13.1	n/a
As originally recorded	6.6	6.9	7.4	8.4	9.5	10.0	11.1	11.6	12.4	13.7

See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

2.7 We would like to draw attention to the following facts:

- For the year ended March 31, 2016 Net Debt increased by \$541.4 million to \$13.7 billion.
- In the ten years reported in Exhibit 2.4, Net Debt

has increased \$7.0 billion.

- The 2016-2017 Main Estimates budgets for an increase in Net Debt of \$468.5 million for the year ended March 31, 2017.
- Based on 2016-2017 Main Estimates, Net Debt of the Province could be in excess of \$14 billion for the year ended March 31, 2017.

Net Debt Growth through Budget Deficits

2.8 Exhibit 2.5 shows the annual budgeted deficit for the Province for the last five years. Even though expenditure growth is slowing, deficits have been budgeted in the last five years which have contributed to Net Debt growth.

Exhibit 2.5 - Annual Budgeted Deficit

Annual Budgeted Deficit					
(\$ millions)					
	2012	2013	2014	2015	2016
Budgeted Deficit	(448.8)	(182.9)	(478.7)	(391.1)	(326.8)

Budget Improvements Required

2.9 The combination of annual budgeted deficits and overruns in budgeted expenses is contributing to the increase in Net Debt. In order to reduce Net Debt, the budgeted deficit needs improvement (i.e. through either increases to revenues, reductions to expenses, or a combination of both). If no other plan of action is taken, the deficit and Net Debt increases will continue.

Budget Plan Forecasts Future Deficits Until 2020-2021

2.10 The government announced in its 2016-2017 budget a multi-year plan to return to a balanced budget state in 2020-2021. This plan includes annual revenue and expense targets, but lacks a Net Debt reduction target.

2.11 The plan indicates from 2016-17 to 2019-2020 annual deficits will be incurred each year, which will further increase the Province's accumulated deficit and Net Debt at the end of fiscal 2019-2020 by a total of \$830 million. In 2020-2021, a surplus is planned of \$21 million. We are very concerned with the government's fiscal plan that continues New Brunswick's Net Debt growth by almost \$1 billion until 2020-2021.

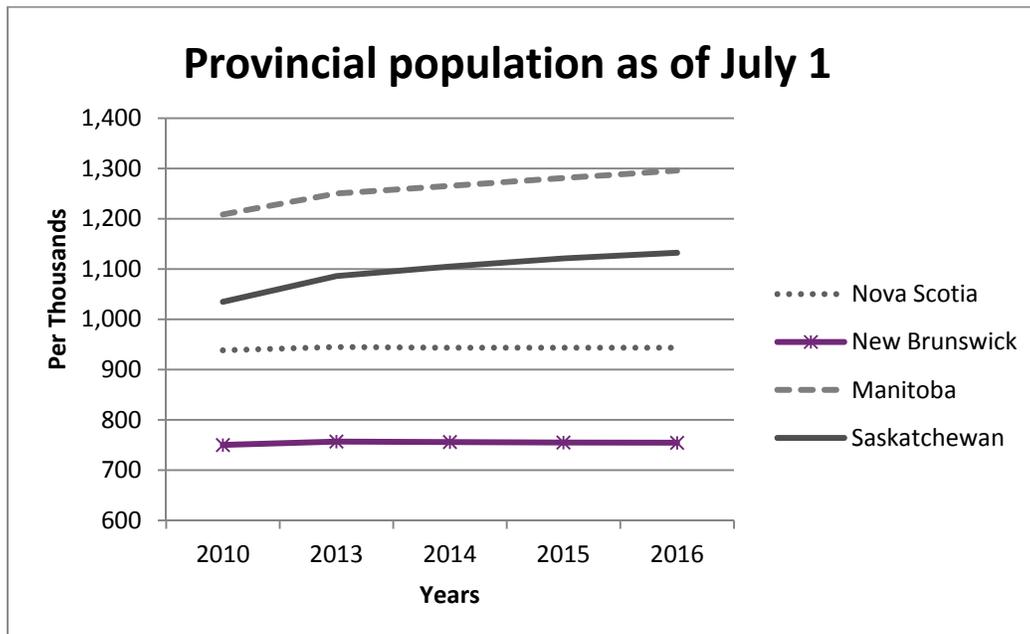
Comparison to Other Provinces

2.12 Another way to assess the significance of the size of the Province's Net Debt is to compare it to the Net Debt of other provinces in absolute amount, per capita and as a percentage of GDP. Provinces used in our comparison include, Nova Scotia, Manitoba and Saskatchewan. These provinces presented for comparison purposes were selected based on application of judgment where certain similarities in population or economic circumstances were considered. The provinces' application of accounting principles may differ upon comparing financial information, depending on particular circumstances. Population data for provinces used in our comparison is found in Exhibits 2.6 and 2.7.

2.13 In the next eight exhibits:

- information from the audited summary financial statements of the individual provinces is used;
- information about population is taken from the Statistics Canada website, and
- GDP figures are from the financial statement discussion and analysis attached to the individual provinces' audited summary financial statements.

Exhibit 2.6 - Provincial Population as of July 1



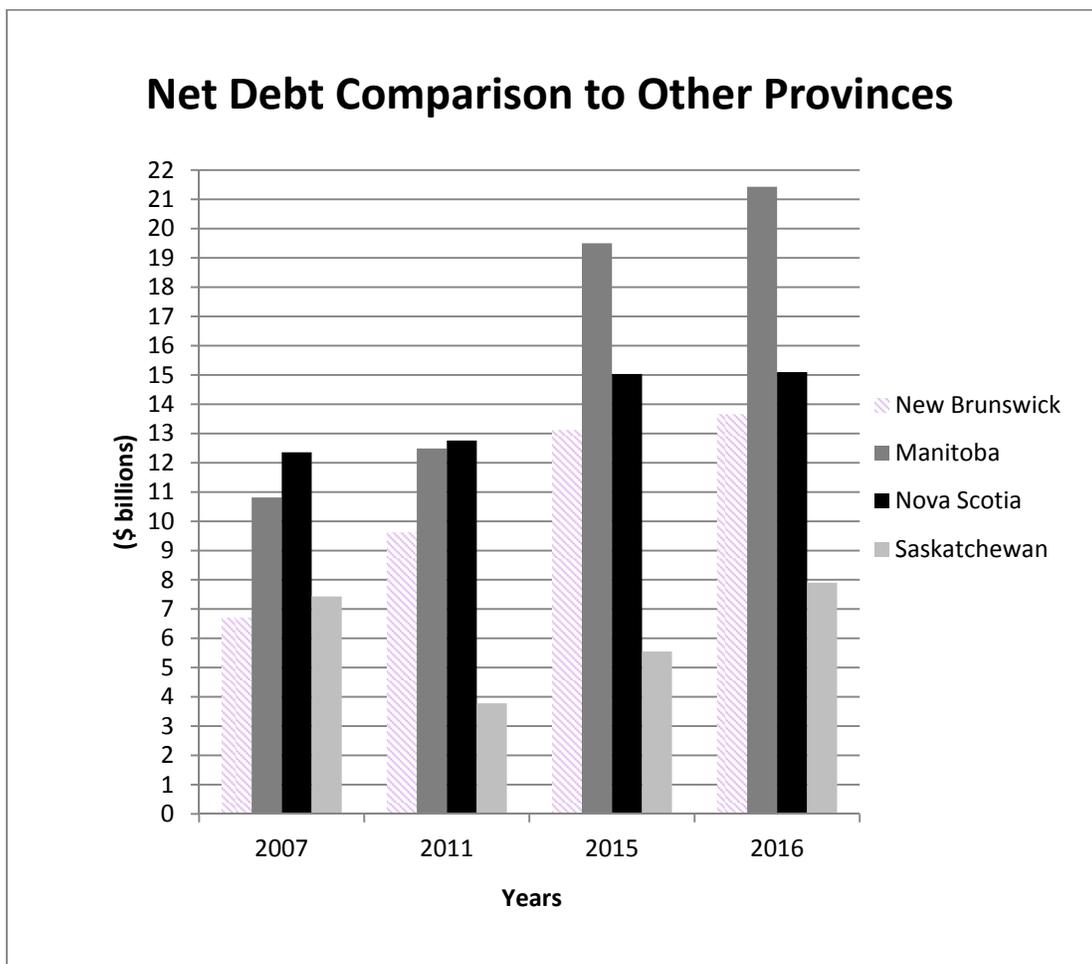
Source: Statistics Canada (filtered data)

<http://www5.statcan.gc.ca/cansim/a26?lang=eng&retrLang=eng&id=0510001&&pattern=&stByVal=1&p1=1&p2=-1&tabMode=dataTable&csid=>

Exhibit 2.7 - Provincial Population as of July 1 Data

Provincial Population Data as of July 1					
Province	(thousands)				
	2010	2013	2014	2015	2016
Nova Scotia	938.2	944.9	943.5	943.3	943.4
New Brunswick	750.0	756.8	755.8	754.9	754.3
Manitoba	1,208.6	1,250.3	1,265.6	1,281.0	1,296.0
Saskatchewan	1,034.8	1,086.0	1,105.0	1,121.3	1,132.3

Exhibit 2.8 - Net Debt Comparison to Other Provinces



See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

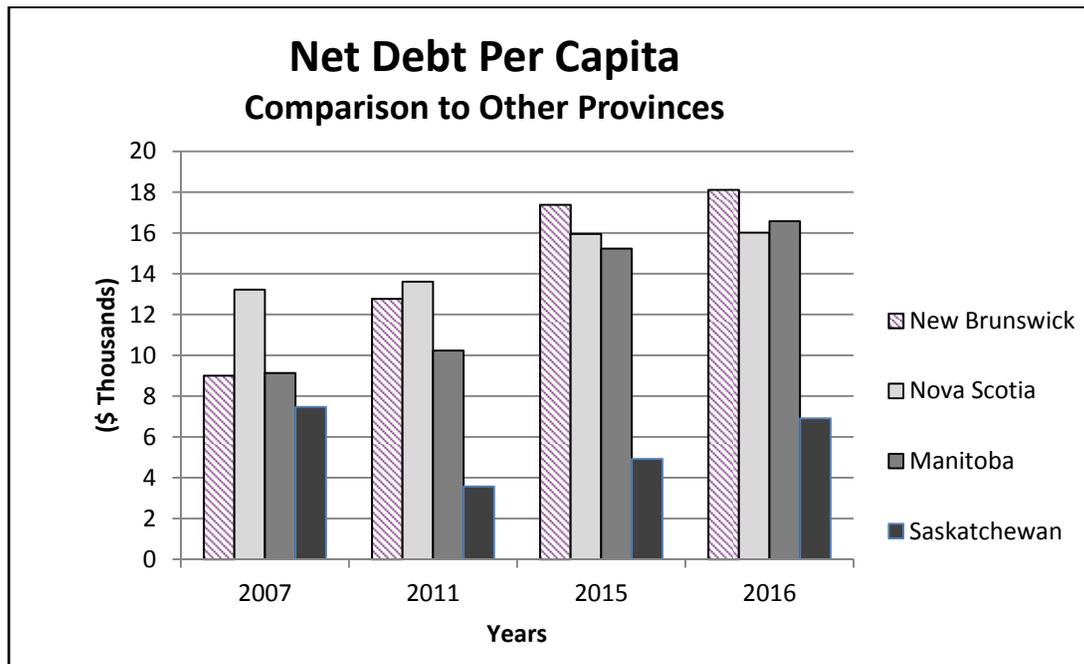
Exhibit 2.9 - Net Debt Comparison to Other Provinces Data

Net Debt Comparison to Other Provinces (\$ billions)					
Province	Increase 2007 to 2016	2007	2011	2015	2016
New Brunswick	104%	6.7	9.6	13.1	13.7
Manitoba	98%	10.8	12.5	19.5	21.4
Nova Scotia	22%	12.4	12.9	15.0	15.1
Saskatchewan	7%	7.4	3.8	5.6	7.9

See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

2.14 Exhibits 2.8 and 2.9 show that over the last ten years within this group, New Brunswick has had the highest increase in Net Debt. New Brunswick's Net Debt has increased by 104% over the last ten years. The magnitude of this increase is significant. The overall debt burden for the Province remains at an elevated level. The 2016-2017 Main Estimates budgets an increase in Net Debt of approximately \$468.5 million. The continued increase in Net Debt causes concern for the long-term sustainability of the Province.

Exhibit 2.10 - Net Debt per Capita Comparison to Other Provinces



See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

Exhibit 2.11 - Net Debt per Capita Comparison to Other Provinces' Data

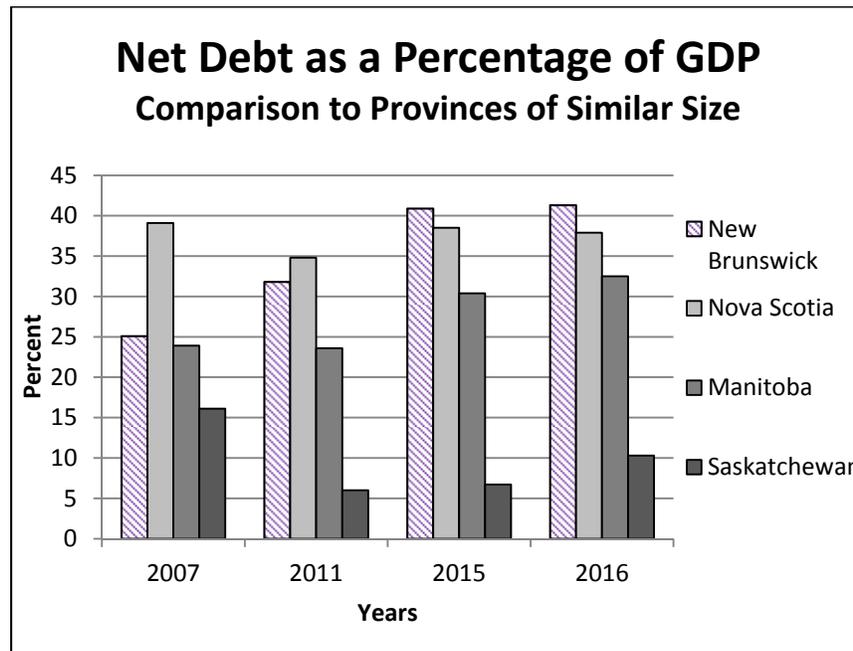
Net Debt Per Capita Comparison to Other Provinces*				
(\$ thousands)				
Province	2007	2011	2015	2016
New Brunswick	9.0	12.8	17.4	18.1
Nova Scotia	13.2	13.7	15.9	16.0
Manitoba	9.1	10.2	15.0	16.3
Saskatchewan	7.5	3.6	4.9	6.9

*Amounts from provinces' 2016 financial statement discussion and analysis where available. For those provinces where this indicator was not published in the same format, information was obtained on population from Statistics Canada as of July 1 within the fiscal year (i.e. 2016 was July 1, 2015 population). Numbers have been rounded for presentation purposes.

See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

2.15 Information in Exhibits 2.10 and 2.11 show that New Brunswick has the highest Net Debt per capita in the comparable group. If the debt were to be eliminated by way of contributions from New Brunswickers, each would contribute \$18,119. Again, this indicator has increased significantly from 2011 at \$12,778 to 2016 at \$18,119 (a 41.8% increase in five years).

Exhibit 2.12 - Net Debt as a Percentage of GDP Compared to Other Provinces



See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

Exhibit 2.13 - Net Debt as a Percentage of GDP Compared to Other Provinces Data

Net Debt as a Percentage of GDP Compared to Other Provinces (percent)					
Province	2007	2011	2015	2016	% Increase (Decrease) from 2007 to 2016
New Brunswick	25.1	31.8	40.9	41.3	16.2
Nova Scotia	39.1	34.8	38.5	37.9	(1.2)
Manitoba	23.9	23.6	30.4	32.5	8.6
Saskatchewan	16.1	6.0	6.7	10.3	(5.8)

See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

2.16 As shown in Exhibits 2.12 and 2.13, New Brunswick had the highest increase of Net Debt as a percentage of GDP from 2007 to 2016, and the highest Net Debt as a percentage of GDP among comparable provinces for 2016. For the year ended March 31, 2007, New Brunswick's result for this calculation was 64.2% of Nova Scotia's; for the year ended March 31, 2016 it was 109.0%.

Net Debt Comparison Summary

2.17 New Brunswick's Net Debt performance compared to other provinces remains a significant concern. New Brunswick's increase in Net Debt of \$7.0 billion from 2007 indicates the need for continued efforts to address the level of Net Debt.

New Brunswick's Credit Rating

2.18 This continued increase in Net Debt represents a very disturbing trend. An even higher demand will exist on future revenues to pay past expenses. Such continued negative trends could have a negative impact on the Province's credit rating (for example, Standard & Poor's decision to downgrade the Province's credit rating from AA- to A+ in 2012.) Downgrades in credit ratings result in more expensive borrowing costs and may constrain future borrowing capacity of the Province.

Exhibit 2.14 shows the Province's credit rating as determined by various credit rating agencies for the past 5 years. All three ratings remained unchanged from previous years and show a stable trend. However, even with stable ratings the Province's borrowing capacity may be negatively affected with New Brunswick's increased debt burden.

Exhibit 2.14 - New Brunswick's Credit Ratings

Year	Dominion Bond Rating Services (DBRS)	Moody's Investors Services	Standard & Poor's
2016	A (high)	Aa2	A+
2015	A (high)	Aa2	A+
2014	A (high)	Aa2	A+
2013	A (high)	Aa2	A+
2012	A (high)	Aa2	A+

2.19 Exhibit 2.15 shows the most recent credit ratings for other provinces compared to New Brunswick. While some provinces have a higher credit rating, overall all provinces noted in Exhibit 2.15 are rated in a good credit quality range.

Exhibit 2.15 - Credit Ratings of Other Provinces

Province	Dominion Bond Rating Services (DBRS)	Moody's Investors Services	Standard & Poor's
New Brunswick	A (high)	Aa2	A+
Nova Scotia	A (high)	Aa2	A+
Manitoba	A (high)	Aa2	AA-
Saskatchewan	AA	Aaa	AA+

Comments on the Province's Financial Health

2.20 For the past number of years, we included in our annual report a historical trend analysis of the Province's financial condition by looking at measures of sustainability, flexibility and vulnerability.

2.21 Starting in 2009, the Province began reporting some of these measures as part of Volume 1 of Public Accounts (Indicators of Financial Health section). As we commented in previous years, we are pleased to see the Province report this historical information.

2.22 In this section, we report on twelve indicators of financial condition identified by the Public Sector Accounting Board (PSAB) in a Statement of Recommended Practice (SORP). This analysis is intended to give a broader view of the financial health of the Province as the analysis shows trends. The analysis expands on the information reported in the audited consolidated financial statements which only reflect the Province's fiscal status at a point in time.

Assumptions Used

2.23 We have not audited some of the numbers used in our indicator analysis; instead, we are using numbers the Province restated as per Note 17 of the Province's consolidated financial statements. The Province used these restated figures in its management discussion and analysis in Volume 1 of Public Accounts. We have not audited the annualized numbers we obtained from the Province for the years 2007 to 2014. For the 2015 to 2016 numbers, we audited the numbers in conjunction with our annual audit work.

2.24 In some of the Exhibits that follow, we show five years of comparative figures instead of ten. For these cases, restated numbers for prior years are not available. As well, in 2016 we updated our chapter format for rounding of numbers. Some minor variances in prior year numbers upon comparison to our prior year report may have occurred in places due to rounding.

Summary of the Province's Indicators of Financial Condition

2.25 In Exhibit 2.16, we summarize our analysis of the Province's financial indicators. We show the indicators for each element, the purpose of the indicator, the short-term (two year) and long-term (five or ten year) trend, as well as a reference within this chapter of where we discuss the indicator in more detail.

Exhibit 2.16 - Summary of Indicators of Financial Condition

	Indicator	Purpose	Short-term Trend	Term	Long-term Trend ¹	Paragraph
Sustainability	Assets-to-liabilities	Measures extent that government finances its operations by issuing debt	Unfavourable	5 year	Unfavourable	2.29
	Financial asset-to-liabilities	Measures whether future revenues will be needed to pay for past transactions	Neutral ²	5 year	Unfavourable	2.31
	Net Debt-to-total annual revenue	Shows whether more time is needed to pay for past transactions	Unfavourable	10 year	Unfavourable	2.33
	Expense by function-to-total expenses	Shows the trend of government spending over time	Neutral	5 year	Neutral	2.35
	Net Debt-to-GDP	Shows the relationship between Net Debt and the activity in the economy	Unfavourable	10 year	Unfavourable	2.39
	Accumulated deficit-to-GDP	Measures the sum of the current and all prior year operating results relative to the growth in the economy	Unfavourable	5 year	Unfavourable	2.41
	Total expenses-to-GDP	Shows the trend of government spending over time in relation to the growth in the economy	Favourable²	10 year	Unfavourable	2.43
Flexibility	Public debt charges-to-revenues	Measures extent that past borrowing decisions limits ability to meet current financial and service commitments	Neutral	10 year	Favourable	2.49
	Net book value of capital assets-to-cost of capital assets	Measures the estimated useful lives of tangible capital assets available to provide products /services	Neutral	5 year	Unfavourable ³	2.53
	Own-source revenues-to-GDP	Measures extent income is taken out of the economy	Favourable²	10 year	Neutral	2.55
Vulnerability	Government transfers-to-total revenues	Measures the dependence on another level of government	Favourable	10 year	Mixed	2.61
	Foreign currency debt-to-Net Debt	Measures the government's potential vulnerability to currency fluctuations	Favourable	10 year	Favourable	2.64

¹Long-term trend assessments unchanged in AGNB Annual Reports 2012-2016, except ratio in paragraph 2.53

²Last year was "Unfavourable"

³Last year was "Neutral"

Conclusion

2.26 The long-term and short-term trends continue to show a number of unfavourable sustainability indicators. Flexibility and vulnerability indicators show more positive results. Overall, eleven of twelve of the Province's long-term indicators of financial condition have remained unchanged since 2012. The other long-term indicator declined in 2016 from neutral to unfavourable. Nine of twelve of the Province's short-term indicators of financial condition have not changed since the prior year. Three short-term indicators showed improvement in 2016.

2.27 We remain concerned about the sustainability indicator trends. The level of Net Debt, now \$13.7 billion, and its increase of over 100% since 2007, is undesirable. This pace of Net Debt growth is not sustainable in the long term, and action is required to address this problem. It may eventually impact the Province's ability to meet its existing financial obligations, both in respect of its service commitments to the public and financial commitments to creditors, employees and others. We again this year, in addition to addressing the annual deficit, encourage the Province to set and achieve targets for long-term Net Debt control and reduction.

Sustainability Indicators

2.28 Sustainability indicates whether the Province can maintain programs and meet existing creditor requirements without increasing the debt burden on the economy.

Assets-to-Liabilities

2.29 The sustainability indicator assets-to-liabilities is presented in Exhibit 2.17.

Exhibit 2.17 - Comparison of Assets-to-Liabilities

Comparison of Assets-to-Liabilities			
Year ended	Total assets (\$ billions)	Total liabilities (\$ billions)	Total assets/ total liabilities (percent)
2012	15.0	17.4	86.2%
2013	15.9	18.7	85.0%
2014	16.1	19.4	83.0%
2015	17.0	21.3	79.8%
2016	17.5	22.2	78.8%

See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

Note: 2014 numbers present audited financial statement figures with no restatements from subsequent years.

2.30 An assets-to-liability indicator below 100% indicates a government has accumulated deficits and has been financing its operations by issuing debt. For the past five years, the Province's rate was less than 100%. Recent trends are negative due to continuous decline in this ratio. Overall we have assessed the short-term and long-term trend as unfavourable.

Financial Assets-to-Liabilities

2.31 Another sustainability indicator, financial assets-to-liabilities, is presented in Exhibit 2.18.

Exhibit 2.18 - Comparison of Financial Assets-to-Liabilities

Comparison of Financial Assets-to-Liabilities			
Year ended	Total financial assets (\$ billions)	Total liabilities (\$ billions)	Total financial assets/ total liabilities (percent)
2012	7.3	17.4	42.0%
2013	7.7	18.7	41.2%
2014	7.8	19.4	40.2%
2015	8.2	21.3	38.5%
2016	8.6	22.2	38.7%

See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

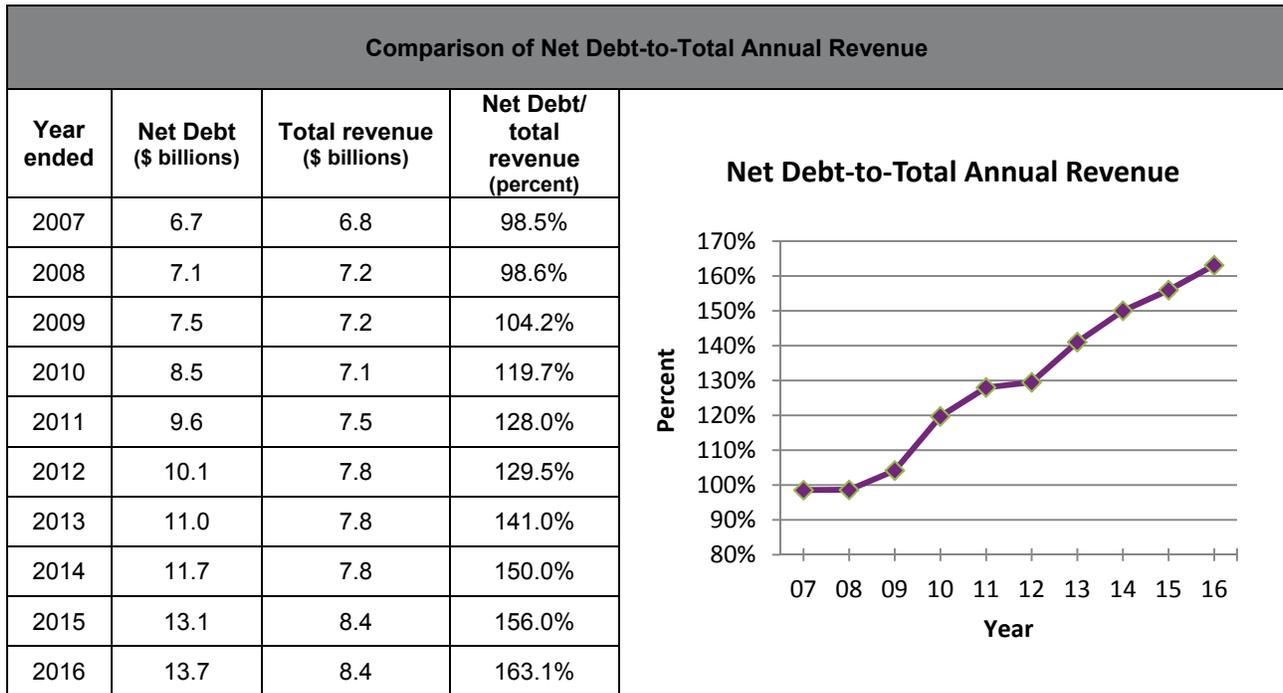
Note: 2014 numbers present audited financial statement figures with no restatements from subsequent years.

2.32 When liabilities exceed financial assets the government is in a Net Debt position, and the implication is that future surpluses will be required to pay for past transactions and events. The Province's percentage overall decreased from 2012 to 2016 indicating liabilities are increasing more than assets. We have assessed the short-term trend as neutral and the long-term trend as unfavourable.

Net Debt-to-Total Annual Revenue

2.33 Net Debt-to-total annual revenue is another indicator of sustainability and is presented in Exhibit 2.19.

Exhibit 2.19 - Comparison of Net Debt-to-Total Annual Revenue



See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

2.34 Net Debt provides a measure of the future revenue required to pay for past transactions and events. A Net Debt-to-total revenue percentage that is increasing indicates that the Province will need more time to eliminate the Net Debt. The Province's percentage has been increasing between 2009 and 2016. The increase in 2013 attributed mainly to the annual deficit and the net capital asset transactions of highways, hospitals, schools and other buildings. Overall, we have assessed this trend as unfavourable.

Expense by Function-to-Total Expenses

2.35 Exhibit 2.20 presents expense by function-to-total expenses.

Exhibit 2.20 - Comparison of Expense by Function-to-Total Expenses

Comparison of Expense by Function-to-Total Expenses										
	2012		2013		2014		2015		2016	
	(\$ billions)	(%)								
Health	2.9	35.8	2.8	33.8	2.9	34.5	2.9	33.0	2.9	33.7
Education and Training	1.7	21.0	1.8	21.7	1.8	21.4	2.1	23.8	1.8	20.9
Social Development	1.0	12.3	1.1	13.3	1.1	13.1	1.2	13.6	1.2	14.0
Service of the Public Debt	0.7	8.6	0.7	8.4	0.7	8.3	0.7	8.0	0.7	8.1
Transportation and Infrastructure	0.5	6.2	0.5	6.0	0.6	7.1	0.6	6.8	0.6	7.0
Central Government	0.5	6.2	0.6	7.2	0.6	7.1	0.5	5.7	0.6	7.0
Protection Services	0.2	2.5	0.2	2.4	0.2	2.4	0.3	3.4	0.3	3.5
Economic Development	0.3	3.7	0.3	3.6	0.2	2.4	0.2	2.3	0.2	2.3
Resources	0.2	2.5	0.2	2.4	0.2	2.4	0.2	2.3	0.2	2.3
Labour and Employment	0.1	1.2	0.1	1.2	0.1	1.2	0.1	1.1	0.1	1.2
Total	8.1	100	8.3	100	8.4	100	8.8	100	8.6	100

See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

2.36 The years ended March 31, 2012 to March 31, 2016 reported deficits. This means that during 2012-2016 while individual expense trends may have remained steady, this result was achieved by incurring a total level of expenses that was in excess of revenue generated in those years. Education and Training and Health's allocation of expenses consume 54.6% of the total expenses, consistent with prior years.

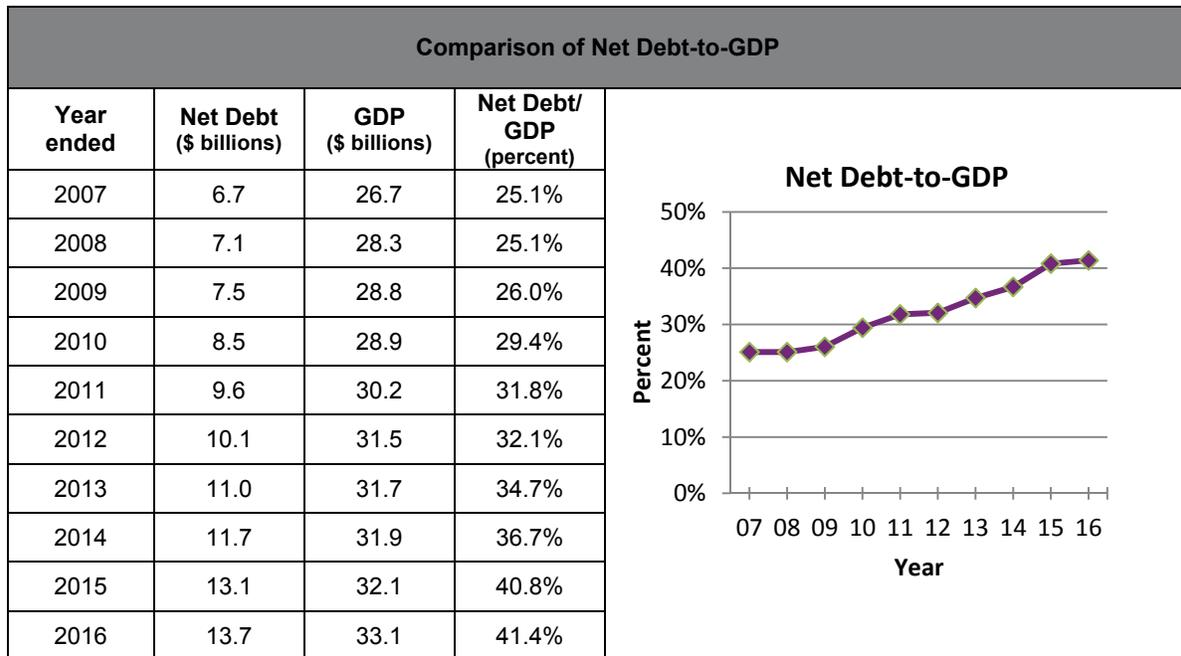
2.37 Also of note is that service of the public debt is now the fourth largest provincial expense category in Exhibit 2.20. Service of the public debt expenses are now larger than each of the following functional areas: transportation and infrastructure, central government, and protection services.

2.38 The allocation of expenses to function when comparing 2016 to other years was relatively stable. The impact of continuing deficits and New Brunswick's growing Net Debt will need to be closely monitored in the future, however, as the related interest burden on the debt consumes resources that would otherwise be used to deliver services. We have assessed this trend as neutral.

Net Debt-to-GDP

2.39 The sustainability indicator, Net Debt-to-GDP is presented in the Exhibit 2.21.

Exhibit 2.21 - Comparison of Net Debt-to-GDP



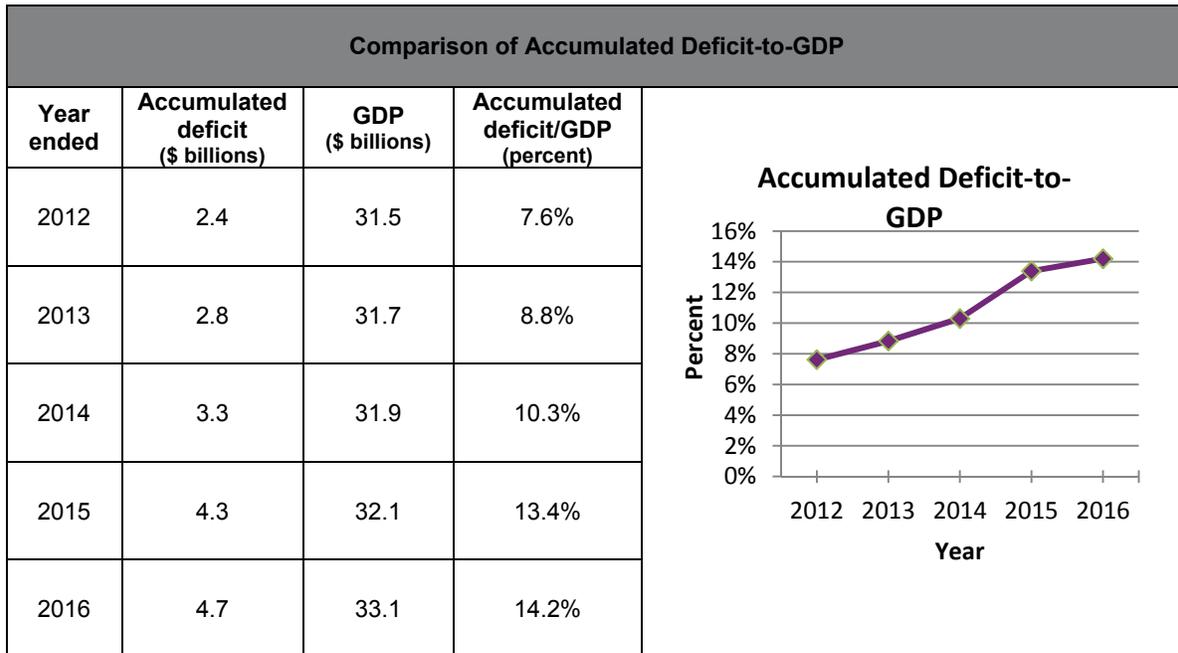
See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

2.40 This indicator compares the Province's Net Debt, the difference between its liabilities and its financial assets, to its GDP. The ratio increased from 2009 to 2016 because the rate of growth of Net Debt exceeded the rate of growth in GDP over that time period. In 2016, the ratio reached its highest level in ten years. This means the Net Debt of the Province is increasing faster than the growth in the economy. We have assessed the trend as unfavourable.

Accumulated Deficit-to-GDP

2.41 In the Exhibit 2.22, we present the sustainability indicator accumulated deficit-to-GDP.

Exhibit 2.22 - Comparison of Accumulated Deficit-to-GDP



See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

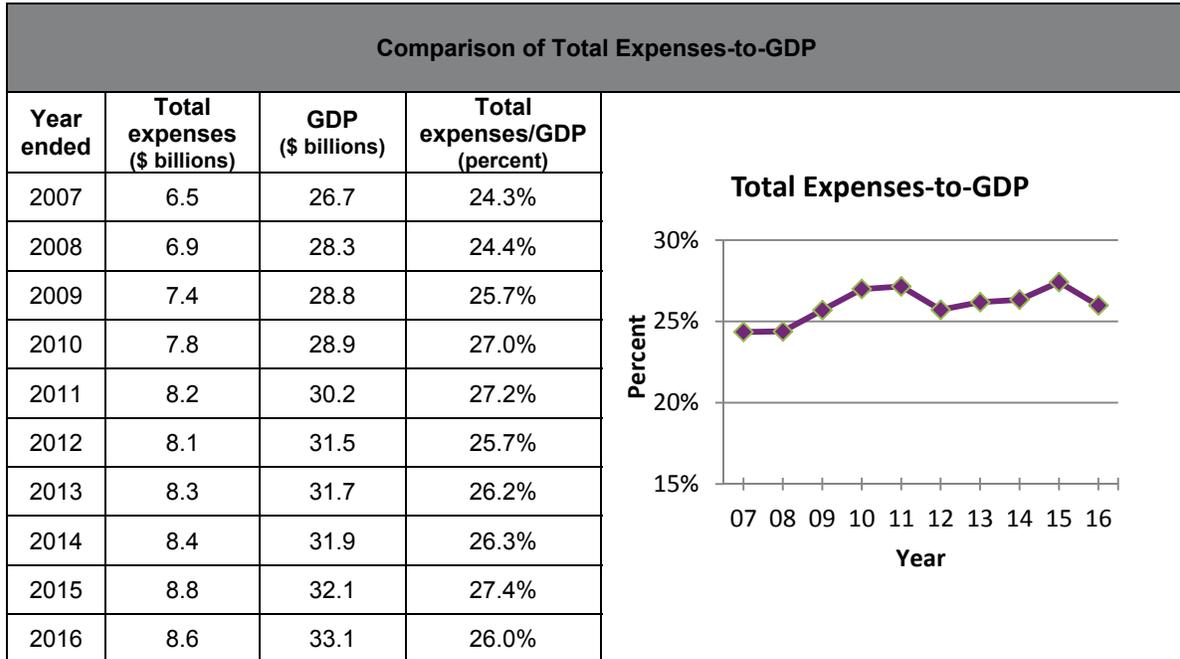
Note: 2014 numbers present audited financial statement figures with no restatements from subsequent years.

2.42 The accumulated deficit is the extent to which annual revenues have been insufficient to cover the annual costs of providing services. The information above shows that from 2012 to 2016, the accumulated deficit has increased faster than the growth of the economy. This represents an unfavourable trend.

Total Expenses-to-GDP

2.43 Exhibit 2.23 presents the total expenses-to-GDP indicator.

Exhibit 2.23 - Comparison of Total Expenses-to-GDP



2.44 Exhibit 2.23 indicates in 2007 and 2008, government expenses were held to about 24% of GDP, however, this percentage has increased over time. In 2016, the percentage decreased slightly from 27.4% in 2015 to 26.0%. In the long term this represents an unfavourable trend as expenses are growing faster than the economy is expanding. In 2016 we have assessed the short term as favourable, given the decline in the 2016 ratio.

Exhibit 2.24 - Sustainability Indicator Trends

Sustainability Indicator Trends		
Sustainability indicator	Short-term trend	Long-term trend
Assets-to-liabilities	Unfavourable	Unfavourable
Financial assets-to-liabilities	Neutral	Unfavourable
Net Debt-to-total annual revenue	Unfavourable	Unfavourable
Expense by function-to-total expenses	Neutral	Neutral
Net Debt-to-GDP	Unfavourable	Unfavourable
Accumulated deficit-to-GDP	Unfavourable	Unfavourable
Total expenses-to-GDP	Favourable	Unfavourable

Summary of Sustainability Indicators

2.45 Exhibit 2.24 presents a summary of the Province's sustainability indicators. We note six of seven sustainability indicators are unfavourable in the long term, and four of seven are unfavourable in the short term, and therefore our overall assessment of these trends remains unfavourable.

2.46 The summary of sustainability indicators is particularly concerning when considering recent important economic events in the Province, all of which are not yet fully reflected in the data presented in this chapter due to timing. Some of these economic events are detailed in the Department of Finance's *Economic Outlook 2016-17*. The following economic events are not considered in the sustainability indicators:

- a significant mine closing and related losses in tax revenue and employment numbers;
- weakening economic forecasts for New Brunswick including declining GDP forecasts;
- demographic changes increasing the need for care services and changing the taxpayer base;
- tax and fee increases including an HST increase; and
- an apparent growing reliance on the Federal government for infrastructure investment and economic growth.

2.47 The Province's financial sustainability remains a significant concern and these overall negative sustainability trends should be of concern to New Brunswickers.

Flexibility Indicators

2.48 Flexibility is the degree to which the government can change its debt or tax burden on the economy to maintain programs and meet existing creditor requirements.

Public Debt Charges-to-Revenues

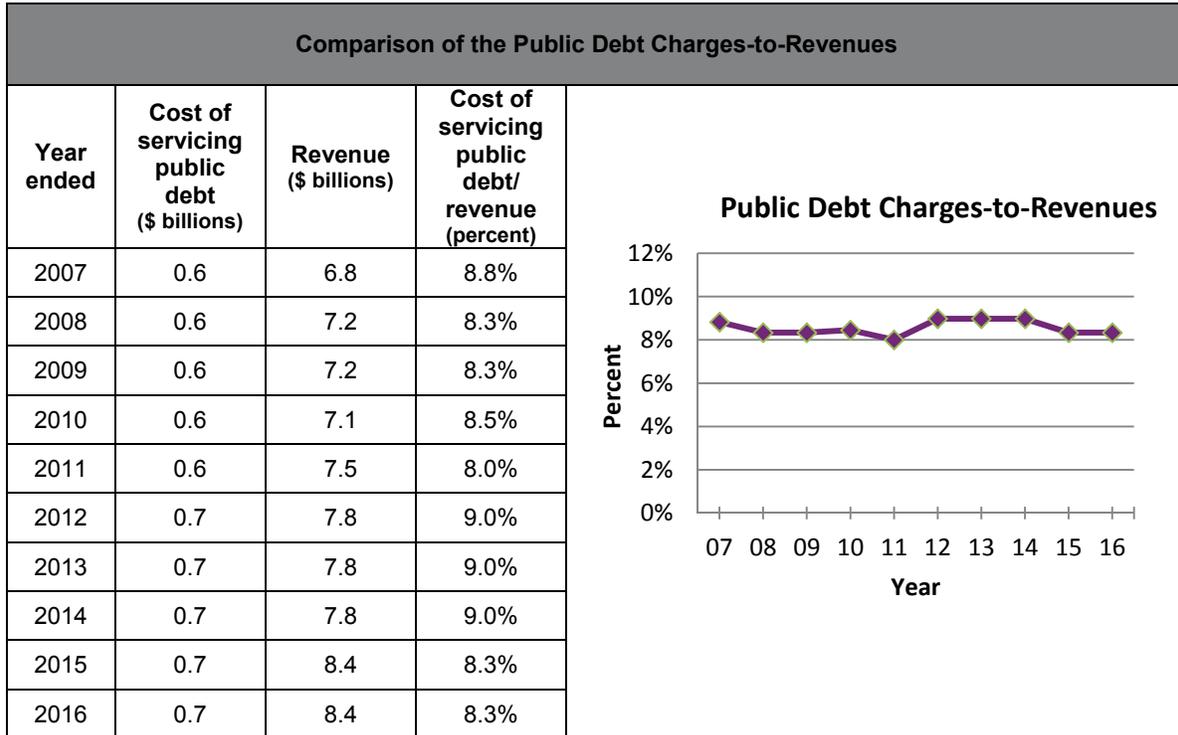
2.49 One of the most publicized factors which affect the flexibility of governments is the cost of servicing the public debt. This is considered to be an indicator of flexibility, since the government's first payment commitment is to service its debt, leaving no flexibility in the timing of these payments.

2.50 The cost of servicing the public debt is comprised mainly of interest on the funded debt of the Province. It also includes foreign exchange paid on interest and maturities during the year, the amortization of foreign exchange gains and losses, and the amortization of discounts and premiums which were incurred on the issuance of provincial debt. It does not include principal repayments on the funded debt of the

Province.

2.51 In Exhibit 2.25, we present the public debt charges-to-revenues.

Exhibit 2.25 - Comparison of the Public Debt Charges-to-Revenues



See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

2.52 Exhibit 2.25 shows that the cost of servicing the public debt as a percentage of the Province's total revenues has remained relatively consistent between 8.0% and 9.0% for the past ten years. We are assessing the short-term trend as neutral. We are assessing the long-term trend as favourable as the 2015 and 2016 ratios are less than the ratio in 2007. A decreasing ratio indicates a favourable trend, as less revenue is needed to service the public debt. Although we are assessing this indicator as favourable, caution is needed when looking at this indicator. The cost of servicing the Province's debt is increasing in a time when interest rates have declined and the Province's debt is increasing significantly.

Net Book Value of Capital Assets-to-Cost of Capital Assets

2.53 We present the net book value of capital assets-to-cost of capital assets in the Exhibit 2.26.

Exhibit 2.26 - Comparison of Net Book Value of Capital Assets-to-Cost of Capital Assets

Comparison of Net Book Value of Capital Assets-to-Cost of Capital Assets			
Year ended	Net book value (\$ billions)	Capital cost (\$ billions)	Net book value/ capital cost (percent)
2012	7.5	12.2	61.5%
2013	8.0	13.1	61.1%
2014	8.0	13.5	59.3%
2015	8.6	14.5	59.3%
2016	8.7	15.0	58.0%

Year	Percent
2012	61.5%
2013	61.1%
2014	59.3%
2015	59.3%
2016	58.0%

See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

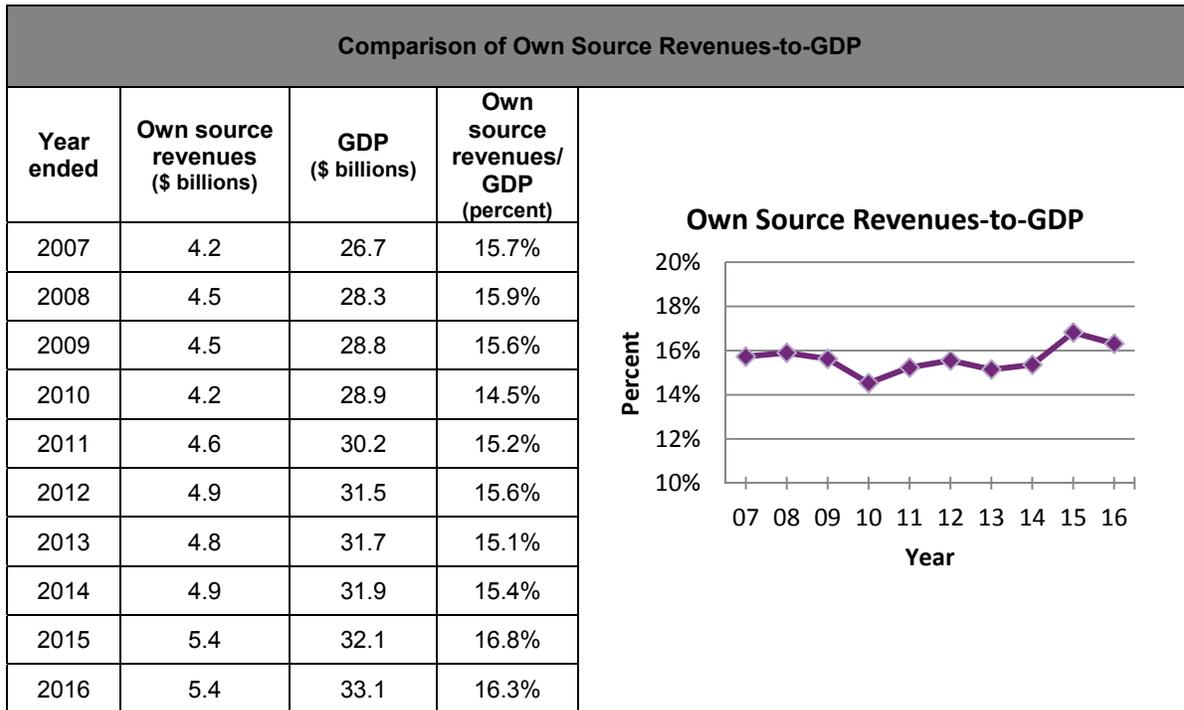
Note: 2014 numbers present audited financial statement figures with no restatements from subsequent years.

2.54 This data indicates that the Province's inventory of capital assets as at March 31, 2016 has 58.0% of its average useful life remaining. This roughly means that on average any provincial assets that were originally expected to be useable for ten years still had just under six years of remaining useful life at March 31, 2016, and assets with original useful lives of twenty years were still considered useable for just under twelve years on average. As the ratios have declined over the past five years, we are assessing the short-term trend as neutral and the long-term trend as unfavourable.

Own Source Revenues-to-GDP

2.55 We present own source revenues-to-GDP in Exhibit 2.27.

Exhibit 2.27 - Comparison of Own Source Revenues-to-GDP



See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

2.56 The own source revenues-to-GDP indicator measures the extent to which the Province is raising its revenue through extracting it from the provincial economy. If the ratio increases, more of the Province's revenue is generated from the provincial economy. For example, an increase in this ratio could result if the Province increased taxes. If the ratio decreases, less of the Province's revenue is generated from the provincial economy. A decreasing ratio increases the Province's ability to raise taxes, thus, making the Province more flexible in how it can generate revenue. Generally, this ratio has stayed the same over the long term and we have assessed this indicator as neutral. In the short term, this ratio is decreasing and we have assessed this trend as favourable.

2.57 There was a decrease in the year 2010 mostly as a result of a large loss by the then New Brunswick Electric Finance Corporation (EFC) (now amalgamated with New Brunswick Power Corporation). In that year, the reduction in own source revenue was not as a result of lower fees or taxes.

2.58 A note of caution should be taken when looking at this indicator for the last eight years. The Province incurred deficits which means expenses were higher than the revenue

generated.

Exhibit 2.28 - Flexibility Indicator Trends

Flexibility Indicator Trends		
Flexibility indicator	Short-term trend	Long-term trend
Public debt charges-to-revenues	Neutral	Favourable
Net book value of capital assets-to-cost of capital assets	Neutral	Unfavourable
Own source revenues-to-GDP	Favourable	Neutral

Summary of Flexibility Indicators

2.59 As summarized in Exhibit 2.28, our overall assessment on flexibility in the short term and long term is mixed. However, caution should be used in interpreting these results. This result occurred in a period where the Province incurred its eighth consecutive deficit and the cost of servicing the Province's debt was increasing (i.e. in a period when interest rates are generally decreasing and the Province's debt load is increasing).

Vulnerability Indicators

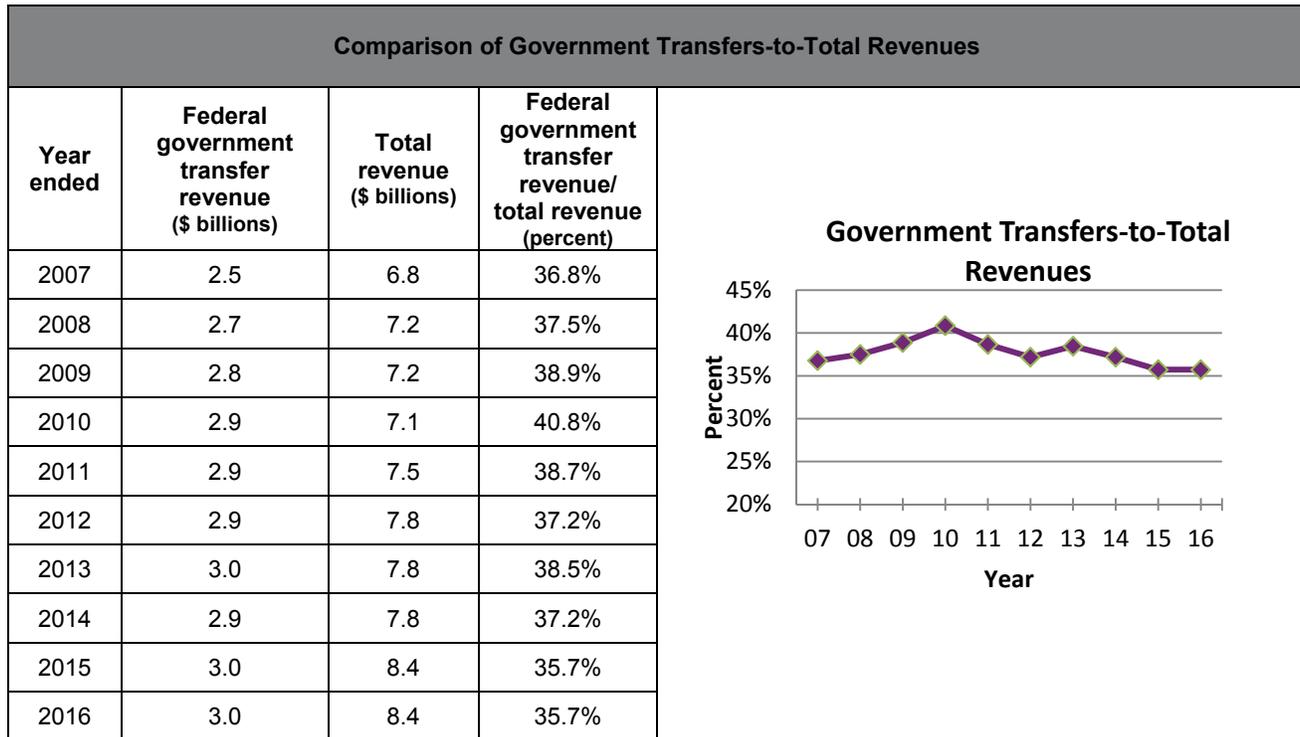
2.60 Vulnerability is the degree to which a government is dependent on sources of funding outside its control or influence.

Government Transfers-to-Total Revenues

2.61 By comparing the proportion of total revenue that comes from the Federal government to the total revenue of the Province, we get a measure of the degree to which the Province is dependent on the Federal government. If that dependence increases, the Province is more vulnerable to funding decisions made by the Federal government.

2.62 Exhibit 2.29 presents the comparison of government transfers-to-total revenues.

Exhibit 2.29 - Comparison of Government Transfers-to-Total Revenues



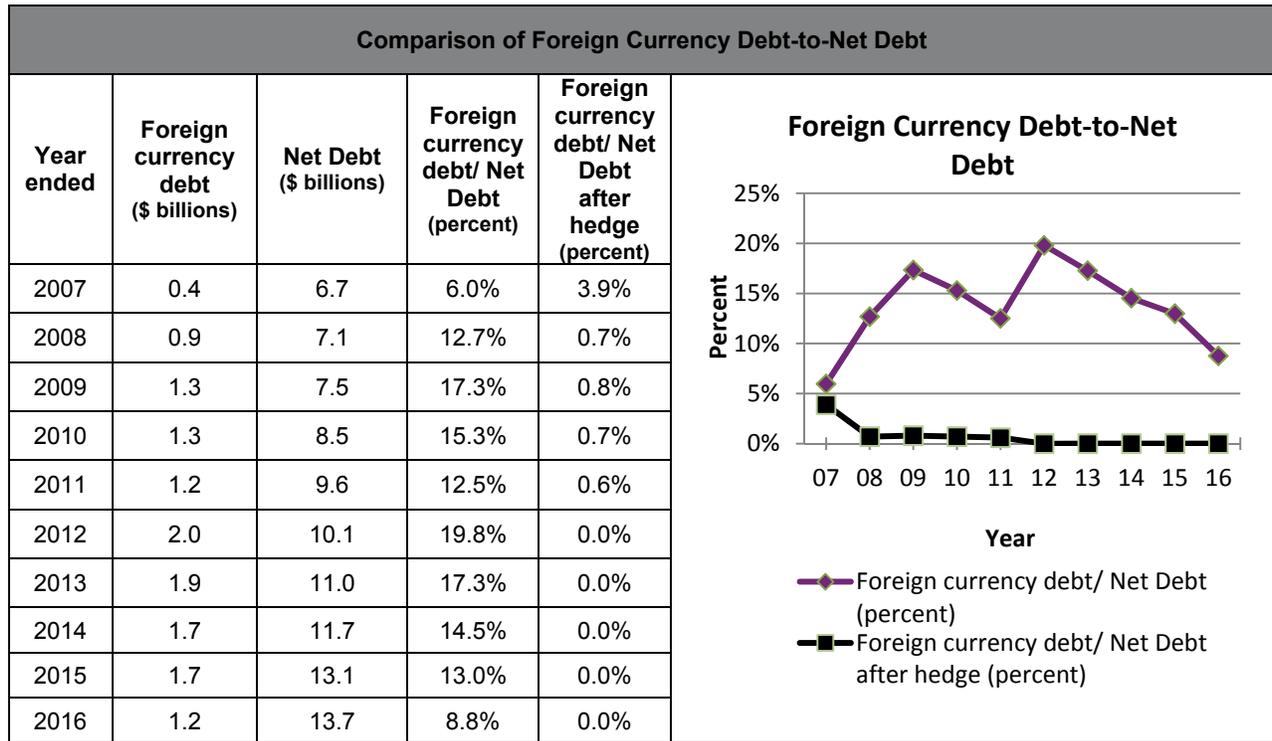
See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

2.63 Exhibit 2.29 shows the Province’s reliance on federal government transfers has been decreasing from 2010. Revenues increased in 2013 in part due to a one-time capital revenue received related to the Route One Gateway Project. The reliance on federal transfers decreased in 2016 and has remained relatively consistent with prior years. Thus we are assessing the short-term trend as favourable and the long-term trend as mixed.

Foreign Currency Debt-to-Net Debt

2.64 The foreign currency debt-to-net debt indicator measures the Province’s potential vulnerability to currency fluctuations and is presented in Exhibit 2.30.

Exhibit 2.30 - Comparison of Foreign Currency Debt-to-Net Debt



See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

2.65 Exhibit 2.30 shows that the Province's foreign currency debt has increased from 2007 to 2012; however foreign currency debt decreased between 2013 and 2016. The risk of exposure to foreign currency fluctuations is offset by the Province's hedging strategy. The Province uses several alternatives to reduce (hedge) risk associated with debt repayable in foreign currencies:

- purchasing assets denominated in foreign currencies for the Province's sinking fund;
- entering into swap agreements which allows repayment of the debt and interest payments in Canadian dollars; and
- entering into forward contracts (which allow the Province to purchase foreign currency at a stipulated price on a specified future date).

2.66 From Exhibit 2.30, we see the risk of exposure to foreign currency fluctuations has decreased significantly over time. Because of the effectiveness of the Province's hedging strategy, we assess this indicator as favourable.

Exhibit 2.31 - Vulnerability Indicator Trends

Vulnerability Indicator Trends		
Vulnerability indicator	Short-term trend	Long-term trend
Government transfers-to-total revenues	Favourable	Mixed
Foreign currency debt-to-net debt	Favourable	Favourable

Summary of Vulnerability Indicators

2.67 As summarized in Exhibit 2.31, the Province's vulnerability exposure is generally favourable. In years when New Brunswick Electric Finance Corporation (now amalgamated with NB Power) generated income through its investment in NB Power, the Province's reliance on federal revenue lessened and this indicator improves. As well, there is reliance on the Federal government in certain years to assist in funding major infrastructure projects. Also of note is that the Province is effectively managing and controlling its exposure to fluctuations in foreign currency.

Comments on Significant Trends Observed in the Province's Consolidated Financial Statements

2.68 In this section, we discuss significant trends we have observed in the Province's consolidated financial statements. We have highlighted these trends to raise public awareness and to provide legislators with an independent assessment of the areas we believe should be a focus for the government.

2.69 For the year ended March 31, 2016, the Province reported a deficit of \$260.5 million. This is a decrease of \$100.9 million from the \$361.4 million deficit reported for the year ended March 31, 2015 (restated).

Deficit

2.70 Exhibit 2.32 shows, at a high level, the reasons for the change in the deficit from March 31, 2015 to March 31, 2016.

Exhibit 2.32 - Analysis of Deficit Decrease

Analysis of Deficit Decrease	
	(millions)
2015 Deficit (restated)	\$(361.4)
Increase in provincial source revenue	4.1
Decrease in federal source revenue	(57.1)
Decrease in expense	153.9
2016 Deficit	\$ (260.5)

2.71 The minor increase in provincial source revenue is a result of increases in Provincial tax revenues of \$46.6 million and increases in other Provincial revenues of \$44.9 million which was offset by a decrease in revenue from NB Power of \$88.0 million.

Expenses

2.72 Total expenses have decreased by \$153.9 million. The most significant decreases in expenses were \$237.4 million in Education and Training. This decrease is mainly due to a one-time pension expense associated with the reform of the teachers' pension plan in 2015. Significant decreases were also noted in Economic Development (\$43.6 million). These decreases were offset by significant increases in Health (\$68.1 million). The increase in Health was mainly the result of additional expenses in the Regional Health Authorities for wages and inflation, along with an increase in payments under the Medicare and drug programs.

2.73 Exhibit 2.33 shows the one year and total annual growth rates in expenses between 2014 and 2016.

Exhibit 2.33 - Expense Trends by Function

Expense Trends by Function							
Function	(\$ millions)			(% percentages)			
	2014 Expenses	2015 Expenses	2016 Expenses	2014 Growth Rate	2015 Growth Rate	2016 Growth Rate	Growth rate 2014-2016
Education and Training	1,836.1	2,083.7	1,846.3	2.7	13.5	(11.4)	0.6
Health	2,786.0	2,830.9	2,899.0	0.0	1.6	2.4	4.1
Service of the Public Debt	661.9	677.2	678.1	0.2	2.3	0.1	2.4
Social Development	1,076.6	1,182.3	1,196.4	2.3	9.8	1.2	11.1
Transportation and Infrastructure	577.9	649.7	636.0	5.5	12.4	(2.1)	10.1
Protection Services	235.2	268.7	281.3	(0.9)	14.2	4.7	19.6
Resources	214.0	197.3	185.3	(12.0)	(7.8)	(6.1)	(13.4)
Central Government	637.1	540.6	585.3	0.1	(15.1)	8.3	(8.1)
Labour and Employment	118.3	122.6	135.0	17.7	3.6	10.1	14.1
Economic Development	231.4	247.6	204.0	(14.0)	7.0	(17.6)	(11.8)
Total	8,374.5	8,800.6	8,646.7				
Total Annual Growth Rate				0.7	5.1	(1.7)	3.3

See paragraphs 2.5 and 2.24 for further information on restatements of prior years.

2.74 Exhibit 2.33 shows the Province's 2016 one-year expense growth rate is (1.7)% compared to the 2014 growth rate 0.7%. In fiscal 2016, six out of ten functions showed an increase in the one year growth rate which implies cost reductions were not realized. Four of ten function areas show a negative growth in 2016 which implies cost reductions were realized. The total expense growth rate between 2014 and 2016 was 3.3% indicating expenses overall are increasing over time.

2.75 We noted the largest decrease in 2016 expense growth rate occurred in the Economic Development and Education and Training areas.

2.76 Exhibit 2.33 shows Labour and Employment experiencing the largest one-year growth rate in 2016 of 10.1%, primarily due to higher expenses resulting from various employment programs. Central Government experienced the second highest growth rate increase due to increased provision expense and increased expenses in General Government.

Revenue

2.77 Exhibit 2.34 shows the one year growth rate and the total annual growth rate of revenue between 2014-2016.

2.78 Total revenues have decreased from 2015 by \$53 million. This is attributable to decreased revenue from federal sources of \$57.1 million and increases in revenue from provincial sources of \$4.1 million.

Exhibit 2.34 - Revenue Trends by Source

Revenue Trends by Source							
Source	(\$ millions)			(% percentages)			
	2014 Revenue Amount	2015 Revenue Amount	2016 Revenue Amount	2014 Growth Rate	2015 Growth Rate	2016 Growth Rate	Growth rate 2014-2016
Provincial Sources							
Taxes	3,595.3	3,983.1	4,029.7	1.5	10.8	1.2	12.1
Licenses and Permits	148.7	149.4	153.8	2.8	0.5	2.9	3.4
Royalties	90.9	97.5	89.3	5.6	7.3	(8.4)	(1.8)
Other Provincial Revenue	856.8	1,003.5	966.6	8.3	16.6	(3.7)	12.8
Sinking Fund Earnings	204.5	195.9	194.1	(7.3)	(4.2)	(0.9)	(5.1)
Federal Sources							
Fiscal Equalization Payments	1,562.0	1,666.0	1,668.0	(2.2)	6.7	0.1	6.8
Unconditional Grants	948.9	955.8	994.7	6.1	0.7	4.1	4.8
Conditional Grants	367.0	388.0	290.0	(27.8)	5.7	(25.3)	(21.0)
Total	7,774.1	8,439.2	8,386.2				
Total Annual Growth Rate				(0.1)	8.6	(0.6)	7.9

As restated

2.79 Exhibit 2.34 shows the Province's 2016 revenue growth rate was (0.6)% which implies revenue is contracting in 2016 compared to 2015. However, from 2014-2016 the Province had a revenue growth rate of 7.9%, which implies overall growth during this time period.

Other Provinces – Revenue and Expense Comparison **2.80** Exhibit 2.35 presents a revenue and expense comparison to certain other provinces.

Exhibit 2.35 - Revenue and Expense (Comparison to other provinces)

Revenue and Expense (Comparison to other provinces)								
(\$ millions)								
	Gross Revenues				Gross Expenses			
	2014	2015	2016	Growth Rate 2014-2016	2014	2015	2016	Growth Rate 2014-2016
New Brunswick	7,774.1	8,439.2	8,386.2	7.9%	8,374.5	8,800.6	8,646.7	3.3%
Nova Scotia	10,060.2	10,661.9	10,937.6	8.7%	10,737.1	10,805.6	10,948.2	2.0%
Saskatchewan	14,418.0	14,058.7	13,633.7	(5.4)%	13,829.0	13,996.8	15,153.2	9.6%
Manitoba	14,414.0	14,963.0	15,054.0	4.4%	14,936.0	15,393.0	15,900.0	6.5%

2.81 Exhibit 2.35 shows New Brunswick's 2014-2016 revenue growth rate was 7.9%, the second highest growth rate for this group. Exhibit 2.35 also shows New Brunswick's 2014-2016 expense growth rate was 3.3%, the second lowest growth rate in gross expenses during this time period.

Exhibit 2.36 – Comparison to Other Provinces – Deficit

Deficit (Comparison to other provinces)				
	(\$ millions)			
	Annual Surplus (Deficit)			
	2014	2015	2016	Growth rate between 2014 and 2016
New Brunswick	(600.4)	(361.4)	(260.5)	(56.6)%
Nova Scotia	(676.9)	(143.7)	(10.7)	(98.4)%
Saskatchewan	589.0	61.9	(1,519.5)	358.0%
Manitoba	(522.0)	(430.0)	(846.0)	62.1%

2.82 As shown in Exhibit 2.36 in comparison to other provinces, New Brunswick has the second largest deficit in 2014 and 2015, and the third largest deficit in 2016. While much has been done to address government expense growth, action is needed still to address New Brunswick's deficit and continued Net Debt growth. Overall, New Brunswick's revenues continue to fall short of its expenses for the eighth consecutive year.

Chapter 3

Accounting for Pensions, Nursing Homes & Contingency Reserve

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Accounting for Pensions, Nursing Homes & Contingency Reserve

Introduction

3.1 In this chapter, our Office (AGNB) presents our observations on the Province's accounting for pensions, nursing homes and the contingency reserve. We believe a separate chapter is needed for these topics because the accounting for pensions, nursing homes and the contingency reserve involves complex accounting issues. Also, in 2016, the accounting for pensions and nursing homes caused significant adjustments to the Province's prior year audited consolidated financial statements.

Accounting for Pensions

3.2 Accounting for pension plans is a complex area requiring significant use of professional judgment. The following paragraphs outline changes which occurred since the 2015 year end audit and are not meant to provide detailed information on pension plan classifications for accounting purposes. Such information can be found in our 2015 Report, Volume III, Chapter 3.

Background

3.3 The Province's March 31, 2015 audited consolidated financial statements contained a qualified audit opinion. This qualified opinion was a result of the Province applying defined contribution accounting for its target benefit pension plans instead of defined benefit or joint-defined benefit accounting. Our view was that defined contribution accounting for these plans represented a departure from Canadian Public Sector Accounting Standards. This departure meant the Province could not receive a clean audit opinion in 2015.

Province changed its accounting policy in 2016

3.4 In 2016 the Province changed its accounting policy for these target benefit pension plans to be in accordance with Canadian Public Sector Accounting Standards. A list of the target benefit pension plans where the Province's accounting changed in 2016 is found in Exhibit 3.1.

Exhibit 3.1 – Pension Plan Accounting Summary 2015-2016

Target benefit pension plan	Province's 2015 accounting treatment	AGNB 2015 & 2016 recommended accounting treatment	Province's 2016 accounting treatment
Public Service Shared Risk Plan (PSSRP)	Defined contribution	Defined Benefit	Defined Benefit
New Brunswick Teachers' Pension Plan (NBTPP)	Defined contribution	Joint Defined Benefit	Joint Defined Benefit
Shared Risk Plan for Canadian Union of Public Employees of NB Hospitals (H-CUPE)	Defined contribution	Joint Defined Benefit	Joint Defined Benefit
Shared Risk Plan for Certain Bargaining Employees of NB Hospitals (H-CBE)	Defined contribution	Joint Defined Benefit	Joint Defined Benefit

Pleased with the 2016 changes

3.5 We were pleased to see the necessary pension accounting changes occurred in 2016 to allow our Office to issue a clean audit opinion on the Province's consolidated financial statements.

Financial impact of the changes

3.6 The primary impact of this pension accounting policy change was a \$224 million increase in liabilities, net debt and opening deficit.

What changed?

3.7 This year, the OOC obtained new information that was not available in the prior year. Specifically, actuarial valuations for accounting purposes using defined or joint defined benefit pension accounting models were obtained for the four target benefit pension plans in Exhibit 3.1.

- New information available*** **3.8** This new information permitted pension accounting calculations to be performed for the Province's financial statements that could not be done in the prior year without this data.
- New accounting questions addressed*** **3.9** As a result of obtaining this new information, additional accounting questions for the Province's target benefit pension plans were able to be considered.
- 3.10** Key questions that were raised and evaluated included:
- the appropriate percentage to include for joint defined plans;
 - the appropriate treatment of the Province's guarantee for the PSSRP;
 - the appropriate amount of indexation to include for target benefit plans; and
 - the appropriate amount of asset to record, if any, for the Province's target benefit pension plans.
- Province's share of joint defined benefit plans*** **3.11** In determining what percentage of the joint defined benefit plan to record in the Province's financial statements, the chief consideration was the intended long-term, and eventual equal sharing of pension contributions between the employer and employee. Therefore, on an overall basis, 50% was supported as the most appropriate portion to include in the Province's financial statements for its joint defined benefit plans.
- 3.12** While current contribution funding does not match a strict 50% employee/employer split, we felt it appropriate to focus on the long term intended plan design of equal contribution sharing. A longer term view helps reduce unnecessary accounting volatility from year to year as contributions levels may fluctuate in the short-term.
- Province's PSSRP guarantee*** **3.13** While there has been no change in the Province's PSSRP guarantee, the appropriate accounting treatment for this guarantee needs to be re-evaluated annually. For this year, we again concluded the Province's treatment of the guarantee through classifying the PSSRP as a defined benefit plan was acceptable, similar to 2014.

3.14 However, as noted in our 2014 Report, Chapter 3, in years immediately following the pension plan conversion, the pension obligation has a high percentage of the pension obligation that is covered by the Province's guarantee. As the guarantee applies to pension benefits earned by all employees and retirees prior to the conversion in 2014, it will lessen with time. For this reason, eventually the classification of this plan may need to be revised to a joint defined benefit plan.

Future indexation of pension benefits

3.15 In determining an estimate of the pension obligation, an important assumption needed was how to account for possible future indexation of pension benefits. Key factors considered include the plan design, actuarial assessments and estimates, and communications to plan members.

3.16 Actuarial work was a very compelling component of the evidence available regarding future pension benefit indexing. Overall, the actuaries calculated the indexing component by estimating the average indexing expected to be provided over the next twenty years. This indexing estimate was included in calculating the pension plan liability.

Amount of pension asset to record for the Province's target benefit plans

3.17 Two of the target benefit plans (PSSRP & NBTPP) were in a net asset position when the accounting calculations were performed as of March 31, 2016. For accounting purposes, a net asset position includes not only pension investment assets in excess of pension liabilities; it also includes deferred losses. (Deferred losses arise when actuarial and experience estimates differ compared to actual results and are deferred and amortized over time).

3.18 Given that the Province has no claim or legal right to target benefit pension plan assets or surpluses, a valuation allowance was applied to remove the value of any remaining pension asset for the target benefit pension plans. This accounting treatment is supported by similar treatment in another jurisdiction, as well as by the Public Sector Accounting Standards.

3.19 The use of a valuation allowance for target benefit pension plans' accounting assets permits a middle ground of accounting to be established. A pension liability can be recorded in years when a net liability exists for accounting purposes, however it also prevents a pension asset from being recorded when it is inappropriate to do so in the Province's target benefit pension plan structure. This approach provides the balance necessary in the Province's target benefit pension plans to consider traditional accounting rules within the new target benefit plan design and structure.

New (ad hoc) audit committee

3.20 We saw this year a new process emerge to address audit issues within the provincial government. An ad-hoc committee was convened in late September 2016 of senior government officials and certain members of Executive Council to discuss significant audit issues at the end of the audit. This process ensured our Office had the opportunity to inform the Committee of significant audit issues where decisions were required, as well as discuss the seriousness and consequences of the pension accounting classification issue.

3.21 Further, in a September 23, 2016 "*Government establishes audit committee*" news release, the government announced the creation of a new audit committee. We understand the current intent is that, as a result of a 2012, 2013, 2014, and 2015 repeated recommendation from our Office, this committee will meet regularly in the future to discuss significant audit issues with key government officials and certain members of Executive Council. We hope the committee, once formalized with a terms of reference or charter, will meet regularly.

Follow up on prior years pension recommendations

3.22 In our 2015 Report, Volume III, Chapter 3 we made seven recommendations regarding pension plans and pension accounting. In 2016, we were pleased to see significant progress in implementing our recommendations.

3.23 Exhibit 3.2 presents the prior year recommendations and their current status. This year, similar to years prior to 2015, we have included any new recommendations concerning pension plans in Chapter 4 where we discuss our significant findings arising from the audit of the Province's financial statements.

Exhibit 3.2 – Summary of Prior Year Pension Plan Recommendations and Current Status

2015 Recommendation	Status in 2016
Unsupported change in pension accounting policy	Implemented
Late accounting decisions	Not implemented
Accounting/documentation concerns with estimates	Not implemented – discussed in Chapter 4
Insufficient audit evidence for the NBTPP assets at conversion date	Resolved
Pension plan financial statements for NBTPP & PSSRP pension plans	PSSRP - implemented
	NBTPP- not implemented
Retirement compensation arrangement concerns	Partially implemented
Lack of rigor in review of pension calculations	Implemented

Progress on 5 of 7 recommendations

3.24 We were pleased to see five of seven recommendations were fully or partially implemented or resolved, however, we would prefer to see all recommendations fully implemented.

Pension plan information

3.25 Exhibit 3.3 provides a summary of pension plan assets, liabilities and expenses for the significant provincial pension plans.

3.26 This information was not included in the Province's financial statements. It had been previously included in the notes to the Province's financial statements in 2014 and prior years. We believe the information in Exhibit 3.3 should be included each and every year to provide more detailed and transparent information to readers of the Province's financial statements. For this year, we have decided to publish the information in our Report to ensure the information is publicly available. Refer to Appendix I for definitions of abbreviations used in Exhibit 3.3.

Exhibit 3.3 - Summary of Significant Pension Plans

Summary of Pension Plan Assets, Liabilities and Expenses (2016)														
in \$ millions														
	PSSRP	NBTPP	H CUPE	H CBE	NH- N&P	NH- G&S	NH- Mgmt	Judges	Members	Sch- Mgmt	Sch- GLTS	Sch- 2745	SERP	Total
Province's Share (per public accounts)	100%	50%	50%	50%	100%	50%	100%	100%	100%	100%	100%	100%	100%	
Plan Assets	6,940.5	2,649.8	359.1	894.4	123.8	211.3	82.7	43.3	-	6.6	341.2	80.0	11.4	11,744.1
Accrued Benefit Obligation	7,188.8	2,510.1	529.6	989.5	126.1	250.2	80.9	84.1	64.1	18.3	397.0	95.9	303.8	12,638.4
Unamortized Adjustments	(451.0)	(84.3)	(23.5)	(19.6)	(6.5)	(14.5)	(4.2)	(5.7)	0.5	-	(31.5)	(10.0)	(30.7)	(681.0)
Valuation Adjustment	202.7	224.0	-	-	-	-	1.8	-	-	-	-	-	-	428.5
Net Benefit Liability	-	-	147.0	75.5	(4.2)	24.4	(4.2)	35.1	64.6	11.7	24.3	5.9	261.7	641.8

Summary of Pension Plan Expenses (2016)														
in \$ millions														
	PSSRP	NBTPP	H CUPE	H CBE	NH- N&P	NH- G&S	NH- MGMT	Judges	Members	Sch- Mgmt	Sch- GLTS	Sch- 2745	SERP	Total
Employers' Share of Benefits Earned	22.8	53.4	22.9	38.8	4.1	10.6	2.3	3.1	-	-	6.8	1.7	8.1	174.6
Net Interest	(5.2)	(19.5)	8.3	4.5	(0.3)	1.4	(0.5)	0.8	1.9	0.7	3.1	0.9	9.3	5.4
Amortization of Adjustments	38.4	5.0	1.7	1.3	(0.4)	(0.3)	(0.5)	1.8	(0.2)	0.3	8.3	2.3	2.6	60.3
Change in Valuation Adjustment	39.0	32.5	-	-	(1.7)	-	(2.3)	-	-	-	-	-	-	67.5
Total Retirement Benefit Expense	95.0	71.4	32.9	44.6	1.7	11.7	(1.0)	5.7	1.7	1.0	18.2	4.9	20.0	307.8

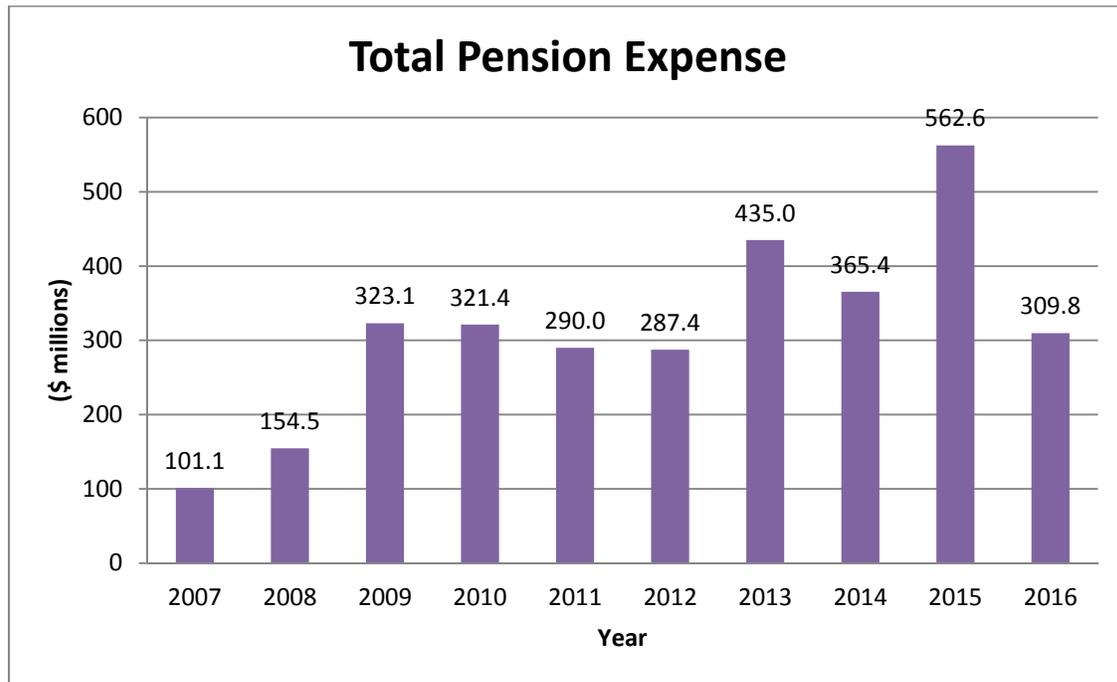
***Pension Expense
and Pension
Contributions***

3.27 Exhibit 3.4 provides details of the Province's total pension expense for the past ten years. For purposes of illustrating the potential volatility of this figure, a longer-term approach of ten years has been provided.

Exhibit 3.4 - Components of Pension Expense

Components of Pension Expense										
(\$ millions)										
	2007	2008	2009	2010	2011	2012	2013	2014	2015 Restated	2016
Employer's share of pension benefits earned	126.1	133.8	146.1	131.6	137.4	148.9	177.4	196.0	161.3	176.6
Net interest expense (revenue)	0.4	(9.1)	20.6	118.2	52.9	32.0	62.7	70.4	38.2	5.4
Plan amendments	5.9	-	-	-	-	-	-	(11.2)	(183.2)	-
Adjustments recognized due to plan amendment	-	-	-	-	-	-	-	-	130.9	-
Amortization of adjustments	(31.2)	30.3	159.7	87.1	99.7	106.5	194.9	132.1	53.4	60.3
Change in valuation adjustment	(0.1)	(0.5)	(3.3)	(15.5)	-	-	-	-	247.0	67.5
Plan settlements <i>(recorded in year as a result of conversion to new pension plan structure)</i>	-	-	-	-	-	-	-	(21.9)	115.0	-
Total pension expense	101.1	154.5	323.1	321.4	290.0	287.4	435.0	365.4	562.6	309.8

Exhibit 3.5 - Total Pension Expense



Pension expense volatility

3.28 Exhibits 3.4 and 3.5 highlight the significant volatility in the annual pension expense over the ten-year period. Pension expense was lowest in 2007 at \$101.1 million and highest in 2015 at \$562.6 million for an increase of \$461.5 million.

Plan settlement pension expenses

3.29 The pension expense for the year ended March 31, 2015 was \$562.6 million, which included a one time plan settlement expense of \$115 million because of the Province's decision to account for the NBTPP using joint defined benefit accounting.

Details of the Province's pension balance

3.30 Exhibit 3.6 provides the history of the Province's pension balance for all pension plans reported in the consolidated financial statements for accounting purposes as well as the important components involved in the pension balance calculation over the past ten years. It is important to note that the pension balance is different than pension expense. In Exhibit 3.6, the pension balance for accounting purposes is the amount that appears on the statement of financial position (or balance sheet) of the Province.

Exhibit 3.6 - Components of the Pension Balance for Accounting Purposes

Components of the Pension Balance for Accounting Purposes										
(\$ billions)										
	2007	2008	2009	2010	2011	2012	2013	2014	2015 Restated	2016
Estimated accrued benefit obligations	7.9	8.3	8.6	8.6	8.9	9.3	10.1	12.3	12.1	12.6
Value of plan assets	8.0	8.0	6.5	7.7	8.4	8.7	9.3	11.5	11.7	11.7
Pension position before accounting adjustments	(0.1)	0.3	2.1	0.9	0.5	0.6	0.8	0.8	0.4	0.9
Accounting adjustments	-	(0.5)	(2.3)	(1.1)	(0.7)	(0.9)	(1.0)	(0.8)	0.2	(0.3)
Pension balance for accounting purposes	(0.1)	(0.2)	(0.2)	(0.2)	(0.2)	(0.3)	(0.2)	0.0	0.6	0.6

Note: 2014 numbers present audited financial statement figures with no restatements from subsequent years

3.31 It should be noted the volatility of the plans would be expected to be reduced over the long term with the introduction of the new shared risk/targeted benefit model, however, the exposure to volatility and risk has not been eliminated.

Pension contribution volatility

3.32 Exhibit 3.7 compares the annual pension expense to the amount of contributions made by the Province to the various pension plans.

Exhibit 3.7 – Pension Expense and Contributions

Pension Expense and Contributions										
(\$ millions)										
	2007	2008	2009	2010	2011	2012	2013	2014	2015 Restated	2016
Pension expense	101.1	154.5	323.1	321.4	290.0	287.4	435.0	365.4	562.6	309.8
Employer contributions	257.7	272.8	288.6	307.8	313.3	327.0	350.8	216.5	260.9	257.2
Excess (deficiency) of employer contributions over pension expense	156.6	118.3	(34.5)	(13.6)	23.3	39.6	(84.2)	(148.9)	(301.7)	(52.6)

Note: 2014 numbers present audited financial statement figures with no restatements from subsequent years

3.33 Exhibit 3.7 shows that for six of the past ten years, the Province’s contributions to its various pension plans have been less than the annual pension expense, whereas four of the past ten years the amount of employer contributions exceeded the amount of the pension expense. Over the past ten years, the Province has contributed \$297.7 million less than the pension expense.

3.34 The significant increase in the deficiency of employer contributions compared to pension expense in 2015 (\$301.7 million) relates to a one time “plan settlement” expense for the NBTPP of \$115 million as a result of the Province’s decision to apply joint defined benefit accounting.

Pension contributions for the Province’s two largest plans

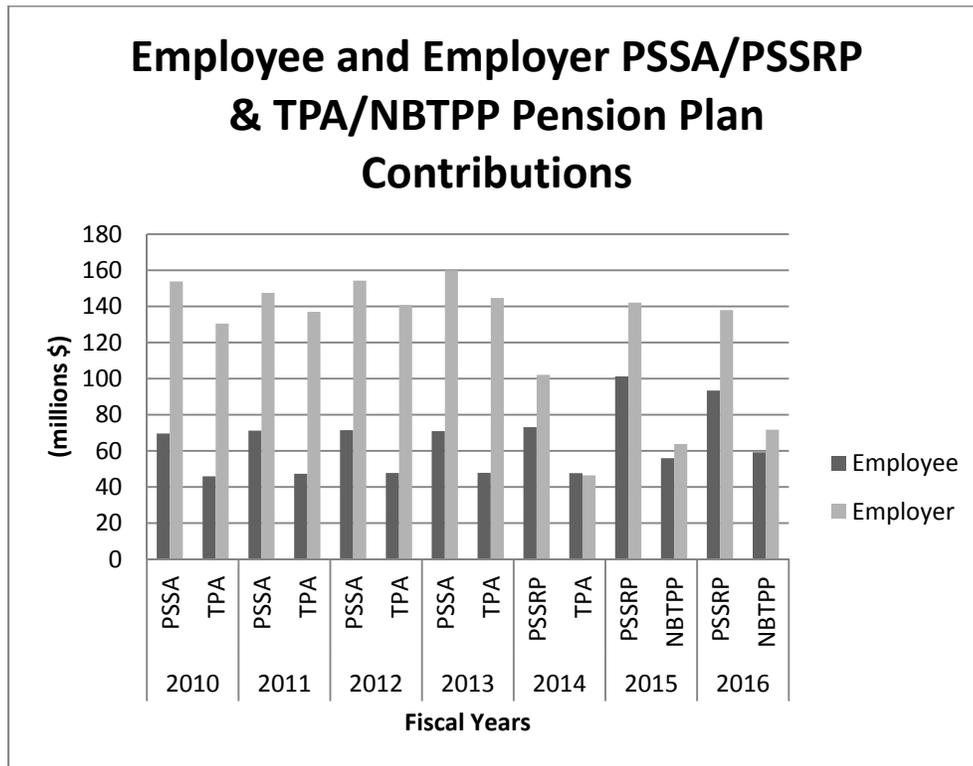
3.35 Further details on pension contributions from 2010 to 2016 for the Province’s two largest plans, the Public Service Superannuation Plan (PSSA), now the PSSRP and the Teacher’s Pension Plan (TPA), now the NBTPP are found in Exhibit 3.8 and Exhibit 3.9.

Exhibit 3.8 – Pension Contributions for the PSSRP/PSSA and NBTPP/TPA Plans

Pension Contributions for PSSRP/PSSA and NBTPP/TPA Plans (\$ millions)							
Fiscal Year	Plan	Employee Contributions	Employer Contributions ¹			Total Employee and Employer Contributions	Ratio of Employer to Employee Contributions
			Normal	Special Payments	Total Employer Contributions		
2016	PSSRP	93.4	138.0	-	138.0	231.4	1.53
	NBTPP	59.2	71.7	-	71.7	130.9	1.28
2015	PSSRP	101.2	142.1	-	142.1	243.3	1.40
	NBTPP	56.0	63.8	-	63.8	119.8	1.14
2014	PSSRP	73.1	102.1	-	102.1	175.2	1.40
	TPA	47.7	46.5	-	46.5	94.2	0.97
2013	PSSA	70.9	92.1	67.9	160.0	230.9	2.26
	TPA	47.9	46.1	98.6	144.7	192.6	3.02
2012	PSSA	71.5	89.4	64.9	154.3	225.8	2.16
	TPA	47.8	46.4	94.4	140.8	188.6	2.94
2011	PSSA	71.2	84.3	63.2	147.5	218.7	2.07
	TPA	47.3	45.1	91.9	137.0	184.3	2.90
2010	PSSA	69.6	92.8	61.0	153.8	223.4	2.21
	TPA	45.9	41.9	88.6	130.5	176.4	2.84
Total 2010-2016	PSSRP	550.9	740.8	257.0	997.8	1,548.7	1.81
	NBTPP	351.8	361.5	373.5	735.0	1,086.8	2.10

¹ PSSRP/PSSA Employer contributions include contributions from the Province, Crown Corporations and other participants.

Exhibit 3.9 – Employee and Employer (PSSRP/PSSA & NBTPP/TPA)



3.36 We noted in Exhibit 3.8, the total employer contributions decreased for the PSSRP by \$4.1 million (3%) and the NBTPP employer contributions increased by \$7.9 million (12%) in fiscal 2016 compared to fiscal 2015. It is important to note that no special payments were made for the PSSRP or the NBTPP/TPA in fiscal 2016, 2015 or 2014.

3.37 In 2015, the \$40.0 million increase in PSSRP (\$17.3 million increase for NBTPP) employer contributions compared to the 2014 results in part relates to an increase in employer contribution rates. Exhibit 3.10 below provides detail on the employer contribution rate changes for the PSSRP and the NBTPP.

Exhibit 3.10 – Employer Pension Contribution Rates

Pension Plan	Employer Rates	
	Prior to New Plan	After New Plan
PSSRP ¹	8.932% up to YMPE ³	12.5%
	11.55% in excess of YMPE	
NBTPP ²	7.3% up to YMPE plus special payments determined by an actuary	11.5% up to YMPE
	9% in excess of YMPE plus special payments determined by an actuary	13.2% in excess of YMPE

¹PSSRP employer contribution rates changed April 1, 2014

²NBTPP employer contribution rates changed July 1, 2014

³YMPE – Yearly Maximum Pensionable Earnings

3.38 As shown in Exhibits 3.8 and 3.9, the total employee contributions increased \$3.2 million (6%) for the NBTPP while the total employee contributions decreased \$7.8 million (8%) for the PSSRP in 2016.

3.39 The ratio of employer to employee contributions for the PSSRP increased from 1.40 in 2015 to 1.53 in 2016. For the NBTPP, the ratio also increased from 1.14 in 2015 to 1.28 in 2016.

Pension Assets Rates of Return

3.40 The net interest component of the pension expense depends primarily on the rate of return earned on pension fund assets. These returns are volatile, as illustrated in Exhibit 3.11 which reports the rates of return for the New Brunswick Investment Management Corporation's (NBIMC) pension funds under management since it was established in 1996 and diversified away from government bonds. The NBIMC serves as trustee and investment manager for the Provincial Court Judges' pension fund, and the investment manager for the PSSRP and NBTPP.

Exhibit 3.11 - NBIMC Rates of Return: Pension funds under management

NBIMC Rates of Return			
Year	Percentage	Year	Percentage
2016	1.66	2006	15.87
2015	14.05	2005	8.51
2014	13.56	2004	25.27
2013	9.08	2003	(6.95)
2012	5.00	2002	3.45
2011	10.42	2001	(5.25)
2010	19.94	2000	20.57
2009	(18.34)	1999	(0.62)
2008	0.79	1998	18.68
2007	8.68	1997	10.14
20 year annualized return			7.20%

3.41 The returns earned by the NBIMC on pension funds under management have ranged from a high of 25.27% in the year ended 31 March 2004 to a low of (18.34) % in the year ended 31 March 2009. Over the past 20 fiscal years the annualized rate of return has been 7.20% for pension funds under management.

Nursing Homes

3.42 In 2016 the Province included for the first time in its financial statements not-for-profit nursing homes operating in New Brunswick. See Exhibit 3.12 for a list of the homes included in the Province's March 31, 2016 consolidated financial statements.

Exhibit 3.12 – Nursing Homes Included in the Province’s March 31, 2016 Financial Statements

Nursing Homes Included in the Province’s March 31, 2016 Financial Statements			
Campbellton Nursing Home Inc.	Campobello Lodge Inc.	Carleton Manor Inc.	Carleton-Kirk Lodge
Central Carleton Nursing Home Inc.	Central New Brunswick Nursing Home Inc.	Dalhousie Nursing Home Inc.	Dr. V. A Snow Centre Inc.
Drew Nursing Home	Forest Dale Home Inc.	Foyer Assomption	Foyer Notre-Dame-de-Lourdes Inc.
Foyer Notre-Dame de Saint-Léonard Inc.	Foyer Saint-Antoine	Foyer Ste-Élizabeth Inc.	Fredericton South Nursing Home Inc. (Pine Grove Nursing Home)
Fundy Nursing Home	Grand Manan Nursing Home Inc.	Jordan Lifecare Centre Inc.	Kennebec Manor Inc.
Kenneth E. Spencer Memorial Home Inc.	Kings Way Care Centre Inc.	Kiwanis Nursing Home Inc.	La Villa Sormany Inc.
Le Foyer St Thomas de la Vallée de Memramcook Inc. – Dr. Camille E. Gaudet	Les Résidences Inkerman Inc.	Les Résidences Jodin Inc.	Les Résidences Lucien Saindon Inc.
Les Résidences Mgr Chiasson Inc.	Lincourt Manor Inc.	Loch Lomond Villa Inc.	Manoir Édith B. Pinet Inc.
Manoir Saint-Jean Baptiste Inc.	Mill Cove Nursing Home Inc.	Miramichi Senior Citizens Home Inc.	Mount St. Joseph of Chatham, N.B.
Nashwaak Villa Inc.	Passamaquoddy Lodge Inc.	Résidence Mgr Melanson Inc.	Rexton Lions Nursing Home Inc.
River View Manor Inc.	Rocmaura Inc.	Tabusintac Nursing Home Inc.	The Church of St. John and St. Stephen Home Inc.
The Salvation Army – Lakeview Manor	Tobique Valley Manor Inc.	Turnbull Nursing Home	Victoria Glen Manor Inc.
Villa Beauséjour Inc.	Villa des Chutes / Falls Villa	Villa du Repos Inc.	Villa Maria Inc.
Villa Providence Shédiac Inc.	Villa St-Joseph Inc.	W.G. Bishop Nursing Home	Wauklehegan Manor Inc.
Westford Nursing Home	White Rapids Manor Inc.	Woolastook Long Term Care Facility Inc (Orchard View)	York Manor Inc.

Background

3.43 In past years, as a matter of routine practice, an accounting assessment has been performed on not-for-profit nursing homes to determine if they need to be included in the Province’s financial statements. In our 2015 Report, Volume III, Chapter 6, we recommended “the Office of the Comptroller (OOC) and the Department of Social Development perform a formal assessment of the substance of provincial activity relating to nursing homes to determine if control for accounting purposes exists under Canadian Public Sector Accounting Standards”. Our office also raised this issue in our 2011 Report, Volume II, Chapter 3.

3.44 It is important to note this assessment is for accounting purposes. Its objective was not to

determine legal control or any other control beyond accounting purposes. This type of assessment is regularly performed by the Office of the Comptroller (OOC) and audited by AGNB for various provincial entities to determine if they need to be consolidated for accounting purposes within the Province's financial statements.

3.45 It is also important to note that this past recommendation applies only to not-for-profit nursing homes in the Province. The Province's for-profit nursing homes operate under a different business structure with less government involvement.

Why did we recommend an accounting assessment for nursing homes in 2015 ?

3.46 In 2015 as we were completing our audit work, we noted a number of new policies and initiatives in the nursing home sector. Some of these activities were as a result of strategic reform or other initiatives. We also became aware of some of this information as a result of a more in-depth review by our Office of the Province's involvement with nursing homes activities.

Implementation of our 2015 recommendation

3.47 In 2016 the OOC followed our recommendation and engaged an expert to complete an accounting assessment. The assessment required significant work and involved analysing several aspects of this complicated accounting question. The results of the assessment concluded that the Province's not-for-profit nursing homes should be consolidated, and therefore the assets, liabilities, revenues and expenses of these nursing homes included in the Province's financial statements.

OOC's accounting conclusion on nursing homes consolidation

3.48 The key reasons the OOC concluded the nursing homes should be consolidated into the Province's financial statements are below:

- 1) The Province's extensive role in determining nursing home budgets, particularly the approval of capital projects;
- 2) The Province's demonstrated role in influencing operating and human resource policies of the homes, such as the mandated staffing skills mix;
- 3) The risk of loss seems to be almost completely borne by the Province—by word, and certainly by past practice;
- 4) The Province's approval and support is

required for nursing homes to borrow funds; and

- 5) The Province's agreement to fund the pension plan deficiency for two out of the three nursing home pension plans for a period of 15 years, exposing the Province to risk of loss.

3.49 Overall there are many parallels in the relationship of the Province with the not-for-profit nursing homes, and the Province's relationship with hospitals (regional health authorities). This would further support that the accounting and reporting for each should be consistent.

3.50 While the nursing homes financial reporting information is not yet available to the level of detail of a regional health authority, the OOC was able to obtain information and record significant nursing home assets, liabilities, revenues and expenses in the Province's financial statements.

3.51 Exhibit 3.13 provides details of the financial impact of consolidating the not-for-profit nursing homes in the Province's financial statements. The data in Exhibit 3.13 includes adjustments to the nursing homes information to be compliant with Public Sector Accounting Standards. Exhibit 3.13 shows the increase in several of the Province's key financial statement balances as a result of the consolidation of nursing homes. This is in addition to the over \$300 million the Province already records annually in its financial statements for nursing home expenses.

Exhibit 3.13 - Financial Impact of Consolidating Not-for-Profit Nursing Homes

Financial Impact of Consolidating Not-for-Profit Nursing Homes		
Increase (Decrease) in \$ millions		
	2015	2016
Assets	37.2	41.3
Non-Financial Assets (e.g. Fixed Assets)	440.3	489.1
Liabilities	559.0	593.2
Net Debt (opening)	497.7	521.7
Accumulated Deficit (opening)	96.9	81.5
Revenues	75.1	85.4
Expenses	59.7*	60.1*

**Note: the above information presents only incremental expenses as a result of the consolidation of nursing homes. This is in addition to the over \$300 million the Province was previously recording annually for nursing home expenses.*

Significant implementation challenges

3.52 While the recommendation was implemented during the 2016 audit year, the implementation was not without significant challenges. These challenges included obtaining comparative (two years) financial information for approximately 60 nursing homes, accounting for employee benefit obligations and harmonizing accounting policies to be compliant with the public sector accounting framework as required in the Province's consolidated financial statements.

Benefits of this accounting change for the Province

3.53 In our view, the inclusion of not-for-profit nursing homes in the Province's financial statements provides more accurate and more complete information about:

- the full obligations of the Province;
- the assets used to provide New Brunswickers services which are largely funded by or through the Province;
- the revenue generated in relation to those services, and
- the expenses incurred to provide those services.

The inclusion of these items in the Province's consolidated financial statements presents a fairer representation of the Province's financial position.

Disappointing nursing home response to OOC requests

3.54 As part of the accounting exercise to record these previously unrecorded nursing home employee benefits liabilities, the OOC requested certain data from nursing homes. Unfortunately only two nursing homes provided the data requested resulting in an increased amount of estimates required in recording nursing homes employee benefit obligations (pension liabilities, retirement allowance obligations, sick leave obligations) in the Province's consolidated financial statements. It also impacted the precision of the employee benefits liability calculation (as the OOC used alternate information to determine appropriate estimates for use in the Province's financial statements). We were disappointed only two nursing homes chose to provide this information to the OOC.

Hopeful for a greater response from nursing homes in the future

3.55 In Chapter 4 of this Volume we have made a recommendation to the OOC to continue to request this information from nursing homes in future years. We hope more homes respond to the OOC request next year.

Contingency Reserve

3.56 As part of its budget for 2016 and 2017, the Province included contingency reserves of \$150 million and \$100 million respectively. As these amounts are significant to the Province's financial statements, we are concerned with how the Province presents this information in its financial statements.

What is meant by the term "contingency reserve"?

3.57 The Province's budgeted contingency reserves do not consist of isolated assets or funds, even though use of the term "reserve" implies some form of an additional source of funds to be used for unexpected program costs. However, there is no such additional fund or reserve; it is simply an amount added to the budget/deficit. As a result, the use of a contingency reserve obscures the true deficit and creates misperception about the Province's true financial state.

Contingency reserve causes unnecessary confusion in reporting the Province's financial results

3.58 Overall, we believe the use of a contingency reserve causes unnecessary confusion in reporting the Province's financial results. The Province's financial results are already complex to interpret and understand. Using a contingency reserve, which allows the Province to fall short on projected revenues or exceed budgeted spending without appearing to go over budget, adds another layer of complexity.

Contingency reserve – budget vs. actuals

3.59 It is the government's prerogative to prepare the budget as it sees fit. However, the actual financial results per the audited financial statements would not recognize such a contingency reserve as a revenue, expense, asset or liability. Therefore Public Sector Accounting Standards do not recognize such a reserve.

Public Sector Accounting Standards require a consistent basis of presentation between budget projections and actual results for valid comparisons

3.60 Under Public Sector Accounting Standards the budget presented in the Province's financial statements needs to be consistent with the accounting used in the Province's financial statements. This is important to ensure readers of the financial statements are able to make valid and legitimate comparisons between budget to actual figures.

Budget presentation differences may be explained in a note to the financial statements

3.61 If the budget as presented in the financial statements is not prepared on the same basis as the actual figures, a reconciliation should be presented in the notes to the financial statements. The reconciliation should identify the approved budget, the actual budget presented in the financial statements, and the show adjustments required between the two.

Pleased with the presentation of the contingency reserve in the Province's 2016 financial statements

3.62 We were pleased the Province did not include the contingency reserve in calculating the annual budgeted deficit in the Province's audited financial statements. We were also pleased the Province included in the notes to its March 31, 2016 consolidated financial statements a reconciliation regarding the budgeted contingency reserve compared to the budget figures presented on the statement of operations.

Will revisit again next year **3.63** We remain concerned about the potential use and presentation of a contingency reserve in the Province’s financial statements, and the confusing or misleading impact it may have on readers or users of the financial statements. We will revisit our examination of this area again in the Province’s March 31, 2017 financial statement audit.

Appendix I – Pension Plan Information

Pension Plan Name Abbreviation	Pension Plan Name	Pension obligations and assets noted in the chapter are measured as at
PSSRP	Public Service Shared Risk Plan	March 31
NBTPP	New Brunswick Teachers' Pension Plan	March 31
H-CUPE	Shared Risk Plan for Canadian Union of Public Employees of NB Hospitals	December 31
H-CBE	Shared Risk Plan for Certain Bargaining Employees of NB Hospitals	December 31
NH-N&P	Pension Plan for Nursing and Paramedical Employees of New Brunswick Nursing Homes	March 31
NH-G&S	Pension Plan for General and Service Employees of New Brunswick Nursing Homes	March 31
NH-Mgmt	Pension Plan for Management Employees of New Brunswick Nursing Homes	March 31
Judges	Provincial Court Act and Provincial Court Judges' Pension Act	March 31
Members	Members' Superannuation Act and Members' Pension Act	March 31
Sch-Mgmt	Pension Plan for Management Employees of New Brunswick School Districts	December 31
Sch-GLTS	Pension Plan for General Labour, Trades and Services Employees of New Brunswick School Districts	December 31
Sch-2745	Pension Plan for Full-Time CUPE 2745 Employees of New Brunswick School Districts	December 31
SERP	Supplementary Retirement Plan	March 31

Chapter 4

**Matters Arising from our
Audit of the Financial
Statements of the Province**

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Matters Arising from our Audit of the Financial Statements of the Province

Province receives clean audit opinion in 2016

- 4.1 On September 27, 2016 the Auditor General signed an unqualified audit opinion on the consolidated financial statements of the Province of New Brunswick.
- 4.2 The opinion indicates the Province's consolidated financial statements are presented in accordance with Public Sector Accounting Standards. We were very pleased to be able to issue an unqualified audit opinion this year.

2015 audit opinion contained reservations

- 4.3 The prior year audit resulted in a serious and disappointing outcome, as the 2015 audit opinion contained reservations regarding the Province's accounting for shared risk pension plans.

New for the Province's financial statement audit in 2016

- 4.4 This year, after much discussion and analysis, the Province changed the accounting classification of its shared risk pension plans in its consolidated financial statements. Also this year, the Province consolidated the balances and transactions for approximately 60 not-for-profit nursing homes, as a result of a new expert accounting assessment.
- 4.5 More information on the Province's accounting for its shared risk pension plans and its consolidation of not-for-profit nursing homes is found in Chapter 3 of this volume.
- 4.6 Significant accounting work and analysis was required to implement both of these accounting changes in the consolidated financial statements and we wish to thank the Office of the Comptroller for its effort and collaboration in both of these areas.

4.7 To reach an opinion on the consolidated financial statements of the Province, we carry out audit work on the major programs and activities in departments. In addition, we audit major revenue items and a sample of expenditures chosen from departments. We also examine internal controls of significant computerized systems.

Audit findings

4.8 In almost every audit, there are audit findings to be discussed with management. The findings from our March 31, 2016 audit were not sufficiently large in dollar or qualitative terms to affect our opinion on the consolidated financial statements. It is our practice to report these matters to senior officials of the departments concerned, and to ask for a response. Our significant findings and recommendations from the audit of the Province's consolidated financial statements with departmental responses are presented in this chapter.

4.9 It should be noted, though, not all findings are included in this Report. In some instances we do not consider the findings to be of sufficient importance to bring to the attention of the Legislative Assembly, or because public attention to internal control weaknesses, before they are corrected, could possibly result in loss of government assets. For further background on our audit objectives refer to Appendix I.

4.10 We had several findings from the March 31, 2016 audit of the Province's consolidated financial statements. We review the findings identified to determine which findings from our work are significant. When considering which findings are significant we assess:

- dollar magnitude of the item;
- the risk the finding could result in a large loss or error in future;
- the number of instances the finding has occurred;
- if the finding has occurred in multiple departments;
- if the finding was reported in a prior year; and
- if we believe the finding is overall significant in nature.

Highlights and Recurring Themes

- 4.11** Highlights and recurring themes of our significant audit findings are presented in Exhibit 4.1.
- 4.12** Overall, we are pleased at the number of prior year audit findings being corrected in 2016. While there remain a number of uncorrected findings, there has been significant progress in implementing our prior year audit recommendations. Areas of improvement in implementing prior years audit recommendations are noted in Exhibit 4.1.
- 4.13** We hope the remaining audit findings are corrected in advance of the next year's audit cycle. Exhibit 4.1 presents the prior year uncorrected findings in shaded boxes.
- 4.14** In addition, we also identified a number of new audit findings in 2016. These are also presented in Exhibit 4.1.

Significant progress in implementation of prior year audit recommendations

Some prior year audit findings remain uncorrected

New audit findings also identified in 2016

Exhibit 4.1 - Highlights and Recurring Themes

Theme	Finding	Finding addressed to	Concern in this area also noted for 2016 AG Report	Concern in this area also noted for 2015 AG Report	Concern in this area also noted in 2014 AG Report	Paragraph Number
Accounting Concerns	Pension accounting – shared risk pension plans	OOC ¹	Improvement	Yes	Yes	2015 Report Chapter 3
	Netting of assets and liabilities	OOC ¹	Yes	No	No	4.72
	Proper and complete accounting for school raised funds	EECD ³	Yes	Yes	Yes	4.79
	Accounting for Nursing Homes	OOC ¹ / SD ⁴	Improvement	Yes	No	2015 Report 6.77 & 6.78
	Liability for contaminated sites	OOC ¹	Yes	Yes	Yes	4.81 & 4.83
	Presentation of Budget Numbers	OOC ¹	Yes	No	No	4.73
	Improper Use of Special Purpose Account	OOC ¹ / SD ⁴	Yes	No	No	4.77
	Nursing Home Pension Plan Classification	OOC ¹	Yes	No	No	4.76
	Approval of Journal Entries	OOC ¹	Yes	No	No	4.82
	Accounting for Province's self-insured WorkSafe liability	OOC ¹	Improvement	Yes	No	2015 Report 6.81
	Accounting for contingent liabilities	OOC ¹	Improvement	Yes	No	2015 Report 6.82
	Classification of accounts in the consolidated financial statements	OOC ¹	Improvement	Improvement	Yes	2014 Report 4.77
	Grants/government transfers – need for accounting analysis	OOC ¹	Improvement	Improvement	Yes	2014 Report 4.79

Shaded findings indicate a concern in this area was also noted in the 2015 or 2014 AG Reports

¹Office of the Comptroller, Department of Finance

²Department of Transportation & Infrastructure

³Department of Education and Early Childhood Development

⁴Department of Social Development

⁵Department of Post-Secondary Education, Training and Labour

⁶Department of Agriculture, Aquaculture and Fisheries

⁷Service New Brunswick (formerly the New Brunswick Internal Service Agency)

⁸Department of Public Safety

Exhibit 4.1 - Highlights and Recurring Themes (continued)

Theme	Finding	Finding addressed to	Concern in this area also noted for 2016 AG Report	Concern in this area also noted for 2015 AG Report	Concern in this area also noted in 2014 AG Report	Paragraph Number
Accounting Concerns (continued)	Tangible capital assets (TCA) – communication of tangible capital asset policy and asset impairment assessment	OOC ¹ /DTI ²	Improvement	Improvement	Yes	2014 Report 4.78
	Property tax revenue - municipal suspense account reconciliations	Finance	Improvement	Improvement	Yes	2014 Report 4.81
	Netting of property tax revenue	Finance	Improvement	Improvement	Yes	2014 Report 4.82
	Support for changes to property tax assessment values	SNB ⁷	Improvement	Improvement	Yes	2014 Report 4.83
Receivables management	Outstanding receivable from 2008 flood	DPS ⁸ /OOC ¹	Improvement	Yes	No	2015 Report 6.83
	Timeliness of property tax receivables processing	Finance	Improvement	Yes	No	2015 Report 6.84
	Property tax accounts receivable balances	Finance	Yes	Yes	No	4.86
	First Nations education – documentation for receivables policy changes	OOC ¹ /EECD ³	Improvement	Yes	No	2015 Report 6.86
Governance/ Oversight Concerns	Lack of an audit committee	Finance	Improvement	Yes	Yes	2015 Report 6.87
	Lack of an internal audit plan	OOC ¹	Improvement	Yes	Yes	2015 Report 6.88
	Need to align Administration Manual Policy AD-6402 – Approval of Payments	OOC ¹ /SNB ⁷	Yes	Yes	Yes	4.78
	Need to complete purchase card policy	OOC ¹	Yes	Yes	Yes	4.85

Exhibit 4.1 - Highlights and Recurring Themes (continued)

Theme	Finding	Finding addressed to	Concern in this area also noted for 2016 AG Report	Concern in this area also noted for 2015 AG Report	Concern in this area also noted in 2014 AG Report	Paragraph Number
<i>Accounting/ Documentation Concerns With Estimates</i>	Nursing Home Employee Benefits	OOC ¹	Yes	No	No	4.74
	Assumptions used by actuaries	OOC ¹	Yes	No	No	4.80
	Write off of accounts and loans receivable	OOC ¹	Yes	Yes	Yes	4.84
	Need to review allowance for doubtful accounts – loans and accounts receivable	OOC ¹ / SD ⁴ / PETL ⁵ / AAF ⁶ / Justice	Improvement	Improvement	Yes	2014 Report 4.75
	Estimate and disclosure of Corporate income tax revenue	Finance	Yes	Improvement	Yes	4.75

4.15 In general, departments' responses indicated they agreed with our recommendations and they intend to address our concerns in the coming year.

4.16 While we have not noted any significant fraud, theft or error as discussed later in Appendix II, the existence of the findings noted in Exhibit 4.1 may increase the risk of loss or mistake in the Province's consolidated financial statements. These items should be addressed prior to the next audit cycle.

Details of Significant Findings

4.17 Our detailed observations, recommendations and departmental responses to our significant findings are presented in Appendix III. Summarized comments pertaining to the key themes of our audit findings are presented in the following paragraphs.

Additional Discussion

4.18 During our 2016 audit of the Province's consolidated financial statements, we noted four themes in our audit findings, all of which were previously reported in either our 2015 or 2014 Annual Reports.

Accounting concerns

4.19 In general, the findings regarding accounting concerns related mostly to appropriate application of accounting standards, accounting errors or other accounting concerns.

4.20 The theme of accounting concerns was notably the area where we saw the greatest implementation of our prior year audit recommendations including: accounting for shared risk pensions, accounting for nursing homes, and accounting for the Province's self-insured WorkSafe liability.

4.21 Prior year accounting concerns in the areas of school raised funds and contaminated sites continue. Also, new in 2016, we had audit findings in areas including: netting of assets and liabilities in the Province's accounts, presentation of budget figures in the audited financial statements and use of special purpose accounts. We hope these new 2016 audit findings are addressed in 2017.

Receivables management

4.22 We noted one audit finding in 2016 related to receivables management. Improvements were also seen in this area compared to the prior year.

4.23 However, we continue to note unfavourable trends and delays in uncollected property tax receivables balances. As this area involves significant balances we remain concerned.

4.24 We are pleased with the progress in implementing audit recommendations from prior years and would like to see the remaining finding addressed for the 2017 audit.

4.25 Overall, we will continue to examine receivables management in our audit processes as it is an important area of good financial management for the Province. An increase or delay in collecting receivables balances of this magnitude represents both increased borrowing costs and expenditures for the Province.

Governance/oversight concerns

4.26 During the Province's 2016 financial statement audit, we noted two findings related to governance/oversight weaknesses, which were previously reported in either our 2015 or 2014 Annual Reports.

4.27 These repeated findings are very concerning given they involve areas with significant provincial expenditures. We will revisit these audit areas again next year. We hope to see these findings addressed prior to the 2017 audit.

4.28 Of particular note in 2016, however, was the Province's implementation of an audit committee. It is very pleasing that this important recommendation dating back to 2012 was implemented. This committee will be a particular benefit in discussing significant audit issues with senior government officials.

***Accounting/
documentation
concerns with
estimates***

4.29 This audit theme had four findings in 2016; three of these findings were new this year. This is somewhat disappointing after last year's improvement in this audit area when there was only one audit finding for this theme.

4.30 Proper support for estimates and assumptions remains an important area of audit focus. Significant management estimates and underlying assumptions need to be well supported with proper rationale, and should include reviewing prior year's estimates to assist in determining estimate accuracy. Evidence of appropriate review for significant judgment areas is also an essential component of an effective internal control system.

4.31 We encourage departments to continue improving in this area.

Information Technology Findings

Auditing the Province's systems and information technology

4.32 In order to express an opinion on the Province's financial statements, we document controls and test transactions processed by significant financial IT systems. Some of this work is performed on a cyclical basis. We also document the controls associated with the Province's overall IT infrastructure. Exhibit 4.2 lists IT systems we examined in the past year.

Exhibit 4.2 - IT work conducted in the past year

Department	IT Work Conducted
Education and Early Childhood Development (EECD)	Teachers' Payroll System
Finance	Property Tax System (Ptax)
Service New Brunswick (SNB) (includes former New Brunswick Internal Services Agency)	HRIS Payroll System (HRIS)
	Oracle Input System (IPM)
	IT Infrastructure
	Property Assessment System (EvAN)
Office of the Comptroller (OOC)	Oracle Financials (Oracle)
Social Development (SD)	Long-term Care System- (NBFamilies)
	Social Assistance Payment System- (NBCase)
Health	Medicare System

Key themes

4.33 We are not publishing the details of all of our IT system work given the technical nature of many of our findings, and as noted previously in this chapter, the risk of possible loss of government assets if the details of such findings are reported. Instead, we are summarizing our findings into key themes by the responsible department. We are reporting this information in Exhibit 4.3.

Exhibit 4.3 - Information Technology Findings – Key Themes

Theme	Finding	Finding addressed to
System replacement	Teachers' payroll system	EECD
	HRIS payroll system	SNB (HRIS)
	Oracle invoice input	SNB (IPM)
Process improvements	Modernization of property assessments	SNB (EvAN)
Segregation of duties	Property tax system	Finance (Ptax)
IT Security	Excessive permissions	Finance (Ptax), SNB (IPM), OOC (Oracle)
	Disabling access	SNB (IT Infrastructure), SNB (EvAN)
	Encryption of data	SNB & DTI (IT Infrastructure)
	Monitoring – Administrators	SNB (EvAN)
	Patch management	OOC (Oracle)
	Management of network access	SNB (IT Infrastructure)
Data integrity/accuracy/ completeness	Exception reports	OOC (Oracle)
	Quality of assessment data	SNB (EvAN)
Non-compliance with policies/standards/guidelines	Assessment re-inspection cycle	SNB (EvAN)
	Annual client reviews	SD (NBFamilies)
	Adult residential certificate of approval	SD (NBFamilies)
Documentation deficiencies	Support for reconciliations	Finance (Ptax)
	Documenting approval	Finance(Ptax)
	Inconsistent payroll documentation	EECD
	Purchase cards – goods received	EECD
	Medicare – physician documentation	Health
Monitoring	Third-party service reports	Health, OOC (Oracle), SNB (IT Infrastructure)
Other observations from our IT work	Business continuity/disaster recovery plan	SNB (HRIS), OOC (Oracle)
	System error	Finance (Ptax)

4.34 We are not aware of any significant loss of government assets or errors which resulted from the findings noted in Exhibit 4.3, however, we are concerned for the potential for future loss of assets or error. Given the findings pertaining to IT security as noted in Exhibit 4.3 we are also concerned

for the potential of loss of confidentiality and privacy inherent in the findings if they remain uncorrected.

4.35 Of particular interest this year, is the number of IT systems needing replacing or modernizing. This number has increased from prior year and we are concerned about the delays in replacing these older systems. In some cases, these systems process vendor payments and provincial payroll which are an essential component of the Province's operations.

4.36 It should be noted, this work was performed with a focus on the financial statement audit impact. Risks arising as a result of operational or confidentiality/privacy concerns are noted where observed, but were not the main focus of our work.

System replacement

4.37 As mentioned earlier, this year we found three IT systems need to be replaced or modernized. Similar to prior year, the EECD teachers' payroll system is still at risk of failure and the SNB (HRIS) payroll system will no longer be supported after 2017.

4.38 This year, the SNB (IPM) system has been added to our system replacement list. IPM is a mission critical system used to enter vendor invoices for payment and it is now no longer fully supported by the supplier. While support has been rarely required in the past, continuing to use unsupported software increases the risk the Province will be unable to process vendor invoices in the future should changes in technology occur.

4.39 All three of these systems will be replaced by one new ERP (enterprise resource planning) system which SNB is responsible for implementing. We are concerned with the lack of progress with this system replacement project. We have received planning information each year on the project, but we have yet to see approval from the Board of Management for funding to commence the project. The latest information we received indicates that approval of funding will be requested in the upcoming budget process.

4.40 As we have mentioned in the past, replacing these outdated systems is critical. For example, the teachers' payroll system access security is extremely weak, support is provided by a single contractor with no backup and the system runs on old, out-dated hardware. The system is over 20 years old and is at risk of failure.

- Process improvements – Property assessments** 4.41 We also noted this year, SNB is modernizing its property assessment system. This modernization project is expected to address the numerous property assessment recommendations we have made in the past and it is expected to be completed as part of a multi-year process. Failure to complete this project in a timely manner will result in the past audit weaknesses continuing until either the modernization is complete or alternative procedures are put in place.
- Segregation of duties** 4.42 This year we had one finding relating to segregation of duties. This finding related to our work in the property tax system where we found one manager was assigned roles for processing transactions and was also responsible for preparing year-end account reconciliations. Having proper segregation of duties helps reduce the risk of fraud and/or error.
- IT security - Excessive permissions** 4.43 We had three findings relating to excessive system access.
- For the property tax system in Finance, we found access to sensitive files was not restricted to only those individuals who require access. The files were stored in a shared location on the network increasing the risk of error or disclosure of potentially confidential information.
 - For the SNB IPM system, we found issues around the use of the administrator account such as external offsite consultants using the administrator account without appropriate monitoring controls or access restrictions. This increases the risk of unauthorized system changes.
 - For the OOC Oracle system, we found the OOC made progress in monitoring the access of the IT support/development team. Additional procedures are required, however, to reduce the risk of inappropriate and unauthorized transactions and/or system changes.
- IT security - Disabling access** 4.44 We noted findings in two of our audits relating to disabling users' system access. Both findings related to SNB. In one case, we found four users continued to have a system owner role after this access had been deemed inappropriate. This access has since been removed. Also for the IT Infrastructure audit, our prior year recommendation on disabling users' access in a timely manner was not implemented.
- 4.45 Timely disabling of user accounts, along with an annual

review of user access assignments, reduces the risk of unauthorized transactions being executed by terminated or existing employees, loss or corruption of data and exposure of confidential corporate information.

***IT security -
Encryption of data***

4.46 We had findings relating to the secure transmission of data in our IT Infrastructure audit. Having appropriate encryption policies in place helps safeguard information and reduces the risk of a breach of confidentiality in the event of unauthorized access to data.

***IT security -
Monitoring
administrators***

4.47 We noted in our SNB property assessment audit, weaknesses in the monitoring of database administrator activity. Database administrators have powerful system access and require proper monitoring controls to reduce the risk of unauthorized changes/updates to significant database tables.

***IT security - Patch
management***

4.48 In our OOC (Oracle) audit, we noted weaknesses in the patch management strategy used to ensure software and databases are running current versions. Failure to have an appropriate patching strategy increases the risk software vulnerabilities could be exploited by outside parties, which could result in loss of information and could impact the stability of systems.

***Data integrity/
accuracy/
completeness***

4.49 We had two findings relating to the integrity, accuracy and completeness of data. One finding related to the accuracy of assessment information recorded in SNB's property tax assessment system. We noted the work of assessors is not reviewed. This lack of review is related to inputting the information into the assessment system. We were informed the new modernization project will address these control deficiencies. Verifying the accuracy of assessment information is required to reduce the risk of inaccurate property assessment values which could result in the over/understatement of provincial revenue.

4.50 The other finding resulted from failure to review exception reports which would identify errors in data transfers between systems. Verifying the accuracy of data transfers helps reduce the risk of error in the accounting records.

Non-compliance with policies/standards/guidelines

- 4.51** In our work, we noted three cases where departments failed to comply with departmental policies/standards or guidelines.
- 4.52** In our audit of SNB property tax assessments, we noted SNB had not visually inspected properties within the timeframe recommended in its departmental guidelines. Completing re-inspections within the appropriate timeframe helps reduce the risk of inaccurate property assessments which would result in provincial tax revenue being over or understated. This control deficiency will be addressed by the property assessment modernization project.
- 4.53** This year in SD, we noted two areas of non-compliance with departmental policy. Not complying with departmental policies increases the risk of SD making ineligible or inaccurate payments.
- We found three in 13 cases examined where annual case reviews were not up-to-date. We noted in two cases, however, the case reviews were subsequently completed.
 - We found one in eight items tested where an adult residential facility did not have a valid certificate of approval for the month tested. A certificate of approval is issued to a facility and renewed annually after the facility is inspected.

Documentation deficiencies

- 4.54** In three audits, we noted documentation deficiencies in our testing. Proper documentation to support transactions provides evidence that transactions are valid and reduces the risk of fraud and error.
- 4.55** In EECD, we were unable to review properly approved payroll documentation to support three of 54 items tested. We also found no evidence goods were received in three of six purchase card transactions tested.
- 4.56** In our testing of 24 Medicare transactions, we noted two cases where documentation was not on file. In one case a physician registration form was not on file, and in the other case, a physician Medicare registration form and signed teletransmission form was not available.
- 4.57** In Finance (Ptax), we noted two areas where documentation was lacking. We found several instances where account reconciliations did not agree with

corresponding general ledger accounts. While these differences were not significant, more diligence and review is required when preparing year-end reconciliations. We also noted Finance does not document its review of the underlying manual calculations for bankruptcies and related write offs.

Monitoring – Third-party service reports

4.58 In three audits, we found cases where departments outsourced services, but did not obtain assurance over the adequacy of controls in place at the service provider. This lack of oversight in relation to services provided by third parties increases the risk critical processes and outsourced controls are not performed in accordance with departments' expectations.

Other observations – Disaster recovery and business continuity planning

4.59 In two audits, we noted issues relating to disaster recovery and business continuity planning. In one case, the plan was out of date and in the other case the plan had not been tested in over three years. Having a documented and tested disaster recovery plan helps ensure systems can be recovered in the event of a disaster.

Other observations – System error

4.60 In Finance (Ptax), we found system errors occur when the system processes certain types of transactions. While these transactions do not regularly occur and cumulatively the dollar value is low, such errors increase the risk of misstatement in the future.

Appendix I - Audit Objectives

4.61 Our examination of the matters included in this chapter of our Report was performed in accordance with Canadian generally accepted auditing standards, including such tests and other procedures as we considered necessary in the circumstances. The matters reported should not be used as a basis for drawing conclusions as to compliance or non-compliance with respect to matters not reported.

4.62 We obtain reasonable assurance on the financial statement figures because it would not be cost effective to obtain absolute assurance - our auditors cannot test every transaction.

4.63 By applying audit procedures to test the accuracy or reasonableness of the figures appearing in the financial statements, we achieve our desired level of assurance. We use audit procedures such as tracing samples of transactions to supporting documents, testing the effectiveness of certain internal controls, confirming year-end balances with third parties and reviewing the reasonableness of estimates.

4.64 Because of the limited objectives of this type of audit work, it may not identify matters which might come to light during a more extensive or special examination. However, it often reveals deficiencies or lines of enquiry which we might choose to pursue in future audit work.

Responsibilities Pertaining to the Audit Process

4.65 The government is responsible for the preparation and the content of the Province's consolidated financial statements. The Statement of Responsibility at the front of Volume 1 of Public Accounts is signed by the Minister of Finance on behalf of the government. The Comptroller is responsible for preparing the financial statements in accordance with Canadian Public Sector Accounting Standards (PSAS). When preparing the financial statements, the government must make significant estimates, as not all information is available or determinable at the time of finalizing the statements. Examples of areas where management has made estimates in the financial statements are: provision for loss on loans and accounts receivable, contingencies, employee future benefits, environmental liabilities, tax revenue reassessments from prior years, tangible capital assets amortization rates and timing of rehabilitation work completed under public private partnership road contracts (which may not reflect when work is actually completed by the contractors and may impact classification of payments as prepaid expenses,

accrued expenditures or tangible capital assets).

4.66 Our Office is responsible for auditing the financial statements. An audit provides reasonable, but not absolute, assurance the Province's financial statements are free of material misstatement. Material misstatement refers to an item or group of items that, if omitted or misstated, would alter the decisions of reasonably knowledgeable financial statement users. The tolerable level of error or misstatement is a matter of judgment.

Appendix II - Loss through Fraud, Default or Mistake

4.67 Section 17(2) of the *Auditor General Act* indicates that the Auditor General may report to the Legislative Assembly cases where fraud or illegal activity has been discovered.

4.68 During the course of our work we became aware of the following losses. Our work is not intended to identify all instances where losses may have occurred so it would be inappropriate to conclude that all losses have been identified.

Department of Natural Resources Missing equipment from various regions	\$ 3,065
Department of Education and Early Childhood Development Missing cash and equipment	\$ 2,150
Department of Transportation and Infrastructure Missing equipment	\$ 54,493
Department of Post-Secondary Education, Training & Labour Missing Cash	\$ 1,640

4.69 Losses reported by our Office only include incidents where there is no evidence of break and enter, fire, or vandalism.

4.70 The Province reports in Volume 2 of the Public Accounts the amount of lost tangible public assets (other than inventory shortages).

4.71 In 2016, the Province reported lost tangible public assets in the amount of \$259,700 compared to a loss of \$21,400 reported for 2015 (revised from \$21,100).

Appendix III - Significant Findings

4.72	Netting of Assets and Liabilities	
<p>As a result of historical accounting practices, loans of \$68.9 million due to Canada Mortgage and Housing (CMHC) relating to not-for profit housing were originally netted against related receivables from the not-for-profit agencies. Current PSAS requires assets and liabilities be reported on a gross basis unless there is a legal right to offset or an entity plans to settle on a net basis. These transactions did not meet these requirements. As a result, the OOC adjusted the Province's financial statements to correct the netted amounts.</p> <p>We are concerned more cases of netting may exist in the Province's financial statements relating to either assets and liabilities or revenues and expenses. This netting would result in an understatement of amounts recorded in the financial statements.</p>		
Recommendation		Comments from Management
<p>We recommend the Office of the Comptroller review the accounting records to determine if other instances of netting exist relating to either assets and liabilities or revenues and expenses. This review should be documented and available for our review.</p>		<p><i>Office of the Comptroller staff identified this issue during the year-end financial statement process and notified the Office of the Auditor General. The instance of netting had been taking place since 1997. Our staff quantified the impact of this item and corrected it in the accounts of the Province.</i></p> <p><i>The Office of the Comptroller does not believe this item is systemic in GNB. As part of the year end process for March 31, 2017, the Office of the Comptroller will ask all departmental accounting staff to review their various programs for instances of netting and report the results of that review to the Office of the Comptroller. This dialogue will be made available to the Office of the Auditor General as the March 31, 2017 audit is being performed.</i></p>

4.73	Presentation of Budget Numbers	
<p>During our audit, we noted the budget figures reported (Main Estimates) on the financial statements were not prepared on the same basis of accounting as the current year numbers reported. Significant differences in presentation between these amounts should be investigated, resolved and presented in a reconciliation in the notes to the financial statements. One example we noted during this year's audit was consolidated nursing home amounts were not included in Main Estimates.</p>		
Recommendation		Comments from Management
<p>We recommend the Office of the Comptroller review the budget numbers reported on the financial statements to determine if the budget is reported on a basis consistent with the actual current year figures. Any differences as required by PSAS, should be explained in the notes to the financial statements.</p>		<p><i>The Office of the Comptroller will review this issue to ensure reporting is in accordance with PSAS.</i></p>

4.74	Nursing Home Employee Benefits	
<p>During this audit, significant progress was made with respect to nursing home consolidation. We noted, however, various assumptions were used by the Office of the Comptroller (OOC) in deriving nursing home accounting estimates. While assumptions are necessary to determine estimates, we found the precision of some of the assumptions could be improved. We noted:</p> <ul style="list-style-type: none"> • the sick leave liability was based on usage data of employees in a similar line of work because this data was not available for nursing home employees; and • the retirement allowance benefit assumed for the Management Group was not supported by an agreement. <p>We recognize consolidating the nursing homes was a significant undertaking requiring many estimates and, in the end, we are comfortable these estimates are not materially misstated. We believe, however, the accuracy of the estimates could be improved if access to detailed data was available.</p>		
Recommendations	Comments from Management	
<p>We recommend the OOC work with nursing homes to obtain sick leave usage and retirement data in order to calculate more precise estimates for the nursing home sick leave and retirement allowance liabilities.</p>	<p><i>The Office of the Comptroller requested data from nursing homes in order to calculate more precise estimates for all areas relating to employee benefit liabilities. The majority of nursing homes advised they were concerned with reporting their information on the books of government given they are independent corporations and to that end, chose not to submit any information. The Office of the Comptroller will continue to make the best possible estimates with the information available.</i></p> <p><i>As this was the first year of the extremely complex process of consolidating nursing homes, the Office of the Comptroller acknowledges there may be potential to improve. Improvement will be made as we refine our methodology based on the information available.</i></p>	

4.75	Estimates and Disclosure of Corporate Income Tax Revenue	
<p>During our audit, we noted documentation deficiencies in the process used to estimate corporate tax revenue. These estimates are a key component in determining provincial corporate income tax revenue which results in approximately \$226 million of provincial revenue.</p>		
<p>The Department of Finance (Finance) does not have a formal documented process for reviewing and approving estimates provided by the Federal government to calculate Corporate Income Tax revenue. We were told these estimates are reviewed, however, evidence of this review is not sufficiently documented. This increases the risk of inaccurate revenues from the Federal government. Given the significance of the revenue involved having an appropriately documented process with proper review is essential to determining an accurate revenue estimate.</p>		
<p>From our review of the financial statement notes, we noted a sensitivity analysis of the corporate income tax revenue is not prepared and the results not disclosed in the financial statements. The sensitivity of these estimates should be disclosed in the financial statement notes in accordance with PS2130. This disclosure should be made given the history of significant year-end adjustments, uncertainty of the estimate submissions and the significant dollar impact if the estimate submissions are adjusted.</p>		
Recommendation	Comments from Management	
<p>We recommend the Department of Finance formally document its process for reviewing and approving estimates provided by the Federal government to calculate Corporate Income Tax revenue. Documented evidence of the approval should be retained for audit purposes.</p> <p>We recommend the Office of the Comptroller disclose the sensitivity of the corporate income tax revenue in accordance with PS2130.</p>	<p><i>The Department of Finance regularly reviews all draft federal estimates relating to the calculation of Corporate Income Tax revenue and is afforded the opportunity to provide input into and verify the official estimate. Confirmation and/or changes are communicated to the federal government by email or verbally. The Department of Finance has documentation on file that supports the estimates used in the calculation of Corporate Income Tax revenue. In order to fulfill this recommendation, the Department of Finance will provide documentation of the approval of estimates with the Federal government going forward.</i></p> <p><i>The Office of the Comptroller will review the reporting of income tax revenue as it relates to PS2130.</i></p>	

4.76	Nursing Home Pension Plan Classification	
<p>During our audit, we noted the Province classified the Pension Plan for General and Service Employees of New Brunswick Nursing Homes (NH-G&S) as a joint defined benefit pension plan. Regardless of demonstrating some of the characteristics of a joint defined benefit plan, the pension plan appears to be sustained by the Province, especially in light of the 2008 Financial Assistance Agreement with the Province to address the going concern funding deficiencies of this plan.</p> <p>We are concerned the significant risks associated with this pension plan are not shared on an equitable basis between the Province and the plan members and that the joint defined benefit classification may not be appropriate for this pension plan.</p>		
Recommendation		Comments from Management
<p>We recommend the OOC prepare a detailed analysis which supports and rationalizes the classification of the Pension Plan for General and Service Employees of New Brunswick Nursing Homes as a joint defined benefit plan. Public Sector Handbook criteria should be supported with evidence in the analysis.</p>		<p><i>The OOC does not share the concern expressed by the Office of the Auditor General and will prepare the detailed analysis requested.</i></p>

4.77	Improper Use of Special Purpose Accounts	
<p>During our audit, we noted the Department of Social Development (SD) appears to have been using the special purpose accounts for Canada Mortgage and Housing (CMHC) to evenly allocate expenses over a period of years. Although listed as CMHC funding in the Special Purpose financial statement note, the amount shown is not actually unspent funds received from CMHC. This “surplus” account is simply an internal mechanism to enable SD to accumulate funds to smooth Provincial contributions as the CMHC funding tapers off over the years. This mechanism enables SD to carry over some of its ordinary budget relating to social housing programs by increasing the amount recorded in special purpose account. The decision on what to allocate the special purpose account is determined annually based on a specific formula rather than on what is actually remains to be spent. This practice has been in place since the start of the agreement.</p>		
Recommendation		Comments from Management
<p>We recommend the OOC investigate whether the Department of Social Development is using the special purpose account appropriately and if the use is not appropriate, the OOC should revise the accounting records so that CMHC amounts are recorded appropriately.</p>		<p><i>The Office of the Comptroller will work with staff at the Department of Social Development to ensure revenues and expenditures relating to the identified program are properly reported.</i></p>
4.78	Need to Align Administration Manual Policy AD-6402 – Approval of Payments	
<p>Again this year, we noted the approval of payments policy AD-6402 and respective processes used at the SNB shared services environment, as well as by other departmental payment systems, are not appropriately aligned. Not following the approved government payment policy increases the risk of payments not being appropriately approved which could lead to invalid payments.</p>		
Recommendation		Comments from Management
<p>We again recommend the OOC and Service New Brunswick work together to update administration manual policy AD-6402 and align the policy and processes to reflect current payment approval requirements for processing government transactions.</p>		<p><i>While there are inconsistencies between the current administrative policy and the payment approval process, given the extent of changes that have occurred recently with the creation of the new Service New Brunswick (SNB), the Office of the Comptroller and SNB have focused their efforts on assessing the adequacy of existing processes and controls in safeguarding the assets of the Province.</i></p>

4.79	School Raised Funds – Communication with Districts	
<p>During our audit of school raised funds, we noted one district, Francophone Nord-Est, was unable to provide supporting backup for school raised funds for the district. We were unable to obtain backup for revenue collected, expenses made or opening and closing bank balances for schools in the district. This is the second year this information was not available. As a result, an estimate of the unsupported amounts was recorded in the Province’s financial statements. Even though we were comfortable with the estimate, not having supporting backup for school raised fund amounts increases the risk of fraud through misappropriation of assets and error in the financial statements.</p>		
Recommendation		Comments from Management
<p>We recommend the Department of Education and the Office of the Comptroller discuss and create a strategy, with representatives of the district Francophone Nord-Est, to obtain supporting backup for school raised fund balances for the district.</p>		<p><i>The Department of Education and Early Childhood Development as well as the Francophone North-East School District agree with this recommendation and are currently working collaboratively to establish a process to ensure backup is available to support revenue and expense transactions as well as opening and closing bank balances. Furthermore, the district is planning to implement a computerized system at the school level (School Cash Net or other) to facilitate the accounting and cash handling processes over school raised funds.</i></p>

4.80	Assumptions Used by Actuaries	
<p>During our audit of pension plans, we made the following observations about the assumptions used by actuaries for calculating financial statement estimates.</p> <ul style="list-style-type: none"> • The assumptions used for the Nursing Home Pension Plans and the Hospital Shared Risk Pension Plans were not reviewed and approved by the Actuarial Valuation Committee (AVC). • The assumptions tended towards the higher end of acceptable ranges for certain discount rates and the inflation rates. • Assumptions approved in advance by the AVC were not re-evaluated at year end to determine if they were still reasonable. • Not all information was considered when assumptions were developed. For example, pay equity amounts were not considered in the salary increase assumption. <p>Assumptions have a significant impact on an actuary's calculations. A small change in an assumption translates to a large fluctuation in the value of an estimate. Each year, we have noted large adjustments to actuarial estimates as a result of actual experience differing from the assumptions used by the actuary. Given this volatile relationship, management should have appropriate oversight and make every effort possible to ensure the accuracy of the assumptions to reduce the risk of inaccurate estimates.</p>		
Recommendation	Comments from Management	
<p>We recommend the OOC review the assumptions approved by the AVC to ensure they are accurate and complete. The assumptions should be based on current relevant data and revised as changes in events occur including significant payroll and economic changes. If the AVC sets assumptions early in the fiscal year, the OOC should review the assumptions to ensure they are still appropriate and consistent at year end.</p>	<p><i>Assumptions approved by the AVC were accurate, complete, and based on current relevant data as at the date of the AVC meeting on March 23, 2016. Changes in circumstances subsequent to year-end resulted in the items 1 and 4 identified above. The assumptions approved by the AVC were within acceptable ranges. Going forward, the OOC will review circumstances closer to the financial statement release date to determine if the approved assumptions remain appropriate.</i></p>	

4.81	Estimates for Remediation of Contaminated Sites	
<p>Estimates of \$33.7 million for future remediation of certain sites in the Province were prepared by the Department of Energy and Resource Development (DERD) and the Department of Transportation and Infrastructure (DTI). During our audit we noted the following:</p> <ul style="list-style-type: none"> • DERD has asserted three independent consultant reports remain an appropriate basis for remediation estimates recorded despite one of the reports dating back to 2011 and another to 2012; however we were unable to view formal documentation analysis to support this rationale; • Of the two older consultant reports, one was issued on an interim basis and not as a final report (DERD); • Estimates prepared using informal information provided by external sources (DTI); and • Estimates recorded at the low end of possible ranges provided by independent consultants without site visits being performed to support the estimate (DTI). <p>While we believe possible differences in these estimates do not represent a material misstatement, a current remediation analysis should be obtained and documented prior to the next year's financial statement audit.</p> <p>We also noted a lack of consistent policy across departments for date of last observation and assessment of site contamination. This inconsistent practice may lead to a risk that determination of the accounting liability is inconsistent or outdated.</p>		
Recommendation		Comments from Management
<p>We recommend the Office of the Comptroller direct the Departments of Energy and Resource Development (DERD) and Transportation and Infrastructure (DTI) to obtain and document current remediation analysis for these mines as soon as possible. Interim reports obtained from independent consultants used in determining a liability for accounting purposes should be obtained in final form.</p> <p>We recommend DERD and DTI perform site visits to support estimates when a range of possibilities has been provided by third parties.</p> <p>We also recommend the Office of the Comptroller, in conjunction with departments, continue to develop a consistent policy to address the date of last site visit that is acceptable for accounting purposes. Guidelines should be provided to the departments to avoid inconsistent or delayed timing in assessing contaminated sites.</p>		<p><i>Canadian public sector accounting standard 3260 allows for the use of alternate means of determining the cost of remediation when the cost of gathering and processing the information required is significant. Subject matter professionals from within the department assess the continuing validity of the most recent environmental assessment reports, and the estimates are adjusted for inflation. The Office of the Comptroller, in conjunction with department professionals, will assess the need for additional assessment activity based upon the specific circumstances surrounding each individual site.</i></p>

4.82	Approval of Journal Entries	
<p>As part of our audit, we tested a sample of thirty journal entries and found two of these journal entries were not properly approved. We saw evidence the OOC communicated the process for approving journal entries with departments. Given the inherent control weaknesses surrounding journal entries, significant risks exist such as fraud and error in the financial records. To reduce these risks, the OOC should communicate again the importance of journal entry approval with departments.</p>		
<p>Although we noted some improvement in this area, lack of journal entry approval has been an issue in our past work. As a result, internal audit should review the journal entry approval process to determine if it is applied consistently and recommend ways the process can be improved.</p>		
Recommendation	Comments from Management	
<p>We recommend the Office of the Comptroller continue to communicate regularly with departments the importance of journal entry approval to reduce the risk of fraud and error in the financial records.</p> <p>We recommend the Office of the Comptroller’s Internal Audit section review the journal entry approval process to determine if it is working appropriately and to suggest ways to improve the consistency of the process.</p>	<p><i>The OOC will continue to communicate regularly with departments regarding the importance of journal entry approval.</i></p>	

4.83	Liabilities for Contaminated Sites – Leased Land	
<p>As we noted in prior year’s audit, the Department of Natural Resources (DNR) and the Department of Agriculture, Aquaculture and Fisheries (DAAF) both lease Crown land. We noted DNR requires lessees to provide insurance for site contamination at the inception of the lease; however DNR does not monitor lessee insurance coverage for compliance after the first year of the lease. DAAF does not ask lessees for evidence of insurance for site contamination. With no insurance in place, there is risk the Province will be liable for any site contamination resulting from use by lessees. During this year’s audit we noted the departments made some progress since our prior year recommendation, however, more work is required by the departments to resolve the issue.</p>		
Recommendation		Comments from Management
<p>We recommend departments obtain evidence of insurance for contaminated sites at the inception of all leases, as well as for each subsequent year the leases are in effect. This review should be documented for audit purposes.</p>		<p><i>The departments have started working towards resolution of this issue and will continue that process.</i></p>
4.84	Write off of Accounts and Loans Receivable	
<p>We noted during our audit, write-offs for accounts and loans receivable are not completed in a timely manner. For example, we found accounts receivable dating back beyond the limitations specified in the <i>Limitations of Actions Act</i> for which the Province would not be able to collect. The <i>Financial Administration Act</i> and the Administration manual policy AD-6307 – Deletion of Debts, require either the Board of Management or Cabinet to approve loan and receivable write-offs. Not writing off of these balances results in an overstatement of gross accounts receivable and allowance for doubtful accounts balances in the Province’s consolidated financial statement note disclosures.</p>		
Recommendation		Comments from Management
<p>We again recommend the Office of the Comptroller amend the <i>Financial Administration Act</i> and Administration Manual policy AD-6307 – Deletion of Debts to enable write-offs of loans and accounts receivable balances to occur in a timely manner.</p>		<p><i>Implementation of this recommendation will have no impact on the net debt or deficit of the Province. As a result of the same finding in the prior year, the presentation of accounts receivable and allowance for doubtful accounts was enhanced to increase the disclosure surrounding these account balances.</i></p> <p><i>The deletion of assets from the accounts of the Province is the responsibility of Board of Management, as prescribed in section 29 of the <i>Financial Administration Act</i>. Administration Manual policy AD 6307, referenced in the Auditor General’s finding, is a policy of Board of Management, prescribed by section 5 (1) (c) of the same Act. While it is possible for the Office of the Comptroller to recommend changes to policies, the authority to amend a policy lies solely with Board of Management.</i></p>

4.85	Incomplete Purchase Card Policy	
<p>We noted the Province does not have a policy in place regarding the use of purchase cards. A new draft policy was completed this year, however, it has not been approved. Given \$32.2 million of government spending is made using purchase cards, a policy should be approved and followed to reduce the risk of fraud or inappropriate use.</p>		
Recommendation	Comments from Management	
<p>We recommend the Office of the Comptroller finalize the purchase card policy in fiscal 2017.</p>	<p><i>The OOC has, after consultation with stakeholders, prepared a draft Purchase Card Policy and intends to present it for approval.</i></p>	

4.86	Collection of Accounts Receivable Balances			
The percentage of property tax accounts in arrears for one year or more (excluding Federal properties) has remained high for the past number of years.				
As at March 31 (in \$millions)				
	2016	2015	2014	2013
Total receivable balance	\$1,089	\$1,087	\$1,028	\$1,004
Total in arrears 1 or more years	\$107	\$108	\$99	\$94
Percentage of arrears 1 or more years	9.8%	9.9%	9.6%	9.4%
March 31 Listing				
	2016	2015	2014	2013
Total number of property accounts	387,030	391,944	382,206	383,672
Total with arrears 1 or more years	54,509	53,213	51,071	56,471
Percentage with arrears 1 or more years	14.1%	13.6%	13.4%	14.7%
Increasing uncollected balances of this magnitude represent both increased borrowing costs and expenditures for the Province.				
Prior to September 2016, the collection of aged accounts receivable was the responsibility of Service New Brunswick (SNB). We were informed the Department of Finance monitored the collection process on a monthly basis and the collection efforts of SNB were not meeting departmental expectations. The collection process did not include setoffs with the Canada Revenue Agency (CRA) and delays in collection activities at Service New Brunswick may have placed certain limitations on the Department's ability to proceed with tax sales. These limitations negatively impacted the Department's ability to recover overdue balances.				
In September 2016, the responsibility for collection of accounts receivable was reassigned to Treasury Board. Given this change in responsibility, discussion is needed between the Department and Treasury Board to align future collection efforts with departmental expectations for property tax accounts receivable.				
Recommendation	Comments from Management			
We recommend the Department of Finance develop an agreement with Treasury Board for the collection of property tax accounts receivable. This agreement should outline the Department's expectations for collection and courses of action should these expectations not be met. The Department should continue to monitor these collection efforts on a monthly basis.	<i>The Department of Finance will continue to monitor its receivable balances on a monthly basis and work with the Treasury Board on an on-going basis to improve the effectiveness of the collection process.</i>			

Chapter 5

Matters Arising from our Audits of Crown Agencies and Federal Claims

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Matters Arising from our Audits of Crown Agencies and Federal Claims

Introduction

- 5.1** In this chapter we discuss our significant findings and recommendations relating to our audits of Crown agencies' financial statements and Federal claims.
- 5.2** We perform an annual financial statement audit for the following Crown corporations, Boards, Commissions, Councils and other agencies:
- Centre communautaire Sainte-Anne (CCSA)
 - Collège communautaire du Nouveau-Brunswick (CCNB)
 - Kings Landing Corporation (KLC)
 - New Brunswick Agricultural Insurance Commission (NBAIC)
 - New Brunswick Community College (NBCC)
 - New Brunswick Highway Corporation (NBHC)
 - New Brunswick Legal Aid Services Commission (LA)
 - New Brunswick Lotteries and Gaming Corporation (NBLGC)
 - New Brunswick Municipal Finance Corporation (NBMFC)
 - Opportunities New Brunswick (ONB)
 - Premier's Council on the Status of Disabled Persons (PCSDP)
 - Public Trustee - Trusts administered (OPT)
 - Regional Development Corporation (RDC)
 - Service New Brunswick (SNB)
- 5.3** We also audit the following Federal claim:
- Agreement Respecting Legal Aid and Court-Ordered Counsel

5.4 To reach an opinion on the Crown agencies' financial statements and Federal claims, we carry out audit work on the major programs and activities in Crown agencies and/or departments. In addition, we audit major transactions and account balances, and examine internal controls of significant computerized systems.

5.5 In almost every audit, matters arise that need to be discussed with management. Except in cases where an audit opinion is qualified, these matters, although significant, are not sufficiently large in dollar or qualitative terms to affect our opinion on the financial statements. Our practice is to report these matters to senior officials of the agencies/departments concerned, and to ask for a response. Some of these findings may not be included in this Report, because we do not consider them to be of sufficient importance to bring to the attention of the Legislative Assembly, or because public attention to internal control weaknesses, before they are corrected, could possibly result in loss of government assets. For further background on our audit objectives refer to Appendix I.

5.6 We are reporting significant audit findings from our past year's audit work. Our findings reported in this chapter depend upon the completion of our audit work relative to the printing of our annual report. Exhibit 5.1 presents the Crown agency financial statement audit work in the last year where findings were noted.

Exhibit 5.1 – Crown Agency with Audit Work in the Last Year Where Findings Were Noted

Crown Agency with Audit Work in the Last Year Where Findings Were Noted	Abbreviation	Financial Statement Year End(s) Completed
Centre Communautaire Sainte-Anne	CCSA	March 31, 2015
Collège Communautaire Nouveau - Brunswick	CCNB	March 31, 2016
Kings Landing Corporation	KLC	March 31, 2015
Legal Aid Services Commission	LA	March 31, 2016
New Brunswick Agricultural Insurance Corporation	NBAIC	March 31, 2015
New Brunswick Community College	NBCC	March 31, 2016
New Brunswick Highway Corporation	NBHC	March 31, 2015
New Brunswick Internal Services Agency (wind up)	NBISA	September 30, 2015
New Brunswick Lotteries and Gaming Corporation	NBLGC	March 31, 2014
Public Trustee - Trusts administered	OPT	March 31, 2015
Regional Development Corporation	RDC	March 31, 2015
Service New Brunswick	SNB	March 31, 2016

5.7 We had several findings from our audits of Crown agencies' financial statements. We review the findings identified to determine which findings from our work are significant. When considering which findings are significant we assess:

- dollar magnitude of the item;
- the risk the finding could result in a large loss or error in the future;
- the number of instances the finding has occurred;
- if the finding has occurred in multiple entities;
- if the finding was reported in a prior year; and
- if we believe the finding is overall significant in nature.

Highlights and Recurring Themes

5.8 Highlights and recurring themes of our significant findings are presented in Exhibit 5.2.

Exhibit 5.2 - Highlights and Recurring Themes

	Crown Agency/ Federal Claim	Concerns in this area noted for 2016 AG Report	Concerns in this area also noted in 2015 AG Report	Concerns in this area also noted in 2014 AG Report
Accounting Concerns	CCNB	Yes	Yes	Yes
	CCSA	Yes		
	Gas Tax	N/A	Yes	
	KLC	Yes	Yes	Yes
	LA	Yes	Yes	Yes
	NBAIC	Yes	Yes	Yes
	NBCC	Improvement	Yes	Yes
	NBHC	Improvement	Improvement	Yes
	NBLGC	Yes	Yes	
	OPT	Yes	Yes	
	PCSDP	*	Yes	
	RDC	Yes	Yes	Yes
SNB	Yes			
Lack of Segregation of Duties	CCNB	Improvement	Yes	Yes
	CCSA	Yes	Yes	
	KLC	Yes	Yes	Yes
	LA	Improvement	Yes	Yes
	NBAIC	Yes	Improvement	Yes
	NBCC	Improvement	Yes	Yes
	OPT	Yes	Yes	
	PCSDP	*	Yes	
	RDC	Improvement	Improvement	Yes
	SNB	Yes		

Shaded Crown agencies indicate a concern in this area was also noted in the 2015 or 2014 AG Reports

*Audit was not completed when exhibit was compiled.

Continued on following page

Exhibit 5.2 - Highlights and Recurring Themes (continued)

	Crown Agency/ Federal Claim	Concerns in this area noted for 2016 AG Report	Concerns in this area also noted in 2015 AG Report	Concern in this area also noted in 2014 AG Report
<i>Oversight/Governance Concerns</i>	CCNB	Improvement	Yes	Yes
	LA	Improvement	Improvement	Yes
	NBAIC	Yes	Yes	Yes
	NBHC	Yes	Yes	
	NBLGC	Yes	Yes	
	OPT	Yes	Yes	
	PCSDP	*	Yes	
	RDC	Yes	Improvement	Yes
	SNB	Yes		
<i>Financial Management/Cash Concerns</i>	CCNB	Yes		
	CCSA	Yes		
	KLC	Yes		
	LA	Yes		
	NBAIC	Yes		
	NBHC	Yes		
	RDC	Yes		
	SNB	Yes		
<i>Accounting/Documentation Concerns With Estimates</i>	CCNB	Improvement	Yes	Yes
	CCSA	Yes		
	NBAIC	Improvement	Yes	Yes
	NBCC	Improvement	Improvement	Yes
	NBHC	Yes	Yes	Yes
	RDC	Yes	Yes	
	SNB	Yes		
<i>Management of Agreements or Third Party Arrangements</i>	CCNB	Yes	Yes	Yes
	NBAIC	Yes	Yes	
	NBCC	Yes	Yes	Yes
	NBLGC	Improvement	Yes	
	SNB	Yes		

Shaded Crown agencies indicate a concern in this area was also noted in the 2015 or 2014 AG Reports

*Audit was not completed when exhibit was compiled.

- 5.9** The data in Exhibit 5.2 does not include Crown agencies or Federal claims we have audited in the past three years, where the Crown agency has now been wound up (Invest New Brunswick and the New Brunswick Internal Services Agency) or for where we no longer perform the financial statement audit or Federal claims audit (e.g. New Brunswick Immigrant Investor Fund (2009) Ltd., Agreement on the Transfer of Federal Gas Tax Revenues).
- 5.10** This year we were engaged to perform the financial statement audit of Service New Brunswick, a new entity resulting from the merger of a number of governmental units. This was a significant undertaking for our Office both in terms of resourcing and volume of work required to complete the audit. The findings from this audit have been included in our analysis in Exhibit 5.2.
- 5.11** We are concerned that a number of these findings in Exhibit 5.2 were observed across different agencies. As a result of the same issue arising in different entities, we saw recurring themes emerge over the course of our work. Exhibit 5.2 shows the agencies/departments where we noted these recurring themes. Due to the significance of the issues and/or the number of instances observed, we have chosen to highlight these recurring themes in this chapter.
- 5.12** Exhibit 5.2 includes a new theme this year which we saw emerge over a number of Crown agency audits: Financial Management/Cash concerns. The new theme occurred because a number of entities had audit findings related to financial management and cash issues. We are concerned at not only the addition of a new theme, but the underlying nature of these audit findings. We will discuss a summary of the findings contained in this new theme later in this chapter.
- 5.13** There were several accounting concerns noted in our Crown agency audits for 2016 involving nine Crown agencies. Seven of these nine Crown agencies also had a finding regarding accounting concerns in either of our 2015 or 2014 Reports. We are pleased to note improvements in two Crown agencies (NBCC, NBHC) where accounting concerns were noted in past.
- 5.14** Accounting concerns should be resolved in advance of our year end audit to ensure the Board or oversight body of the Crown agency receives accurate and complete financial information during the year.

***Accounting
concerns***

5.15 We noted accounting concerns most often related to inadequate support for accounting balances and reconciliations, deficiencies with Crown agencies internal accounting policies or processes, as well as management not being aware of changes to accounting standards or not applying new accounting standards properly. We also noted instances where Crown agencies had inconsistent accounting policies for different internal units as well as inefficient systems and processes for financial statement preparation.

5.16 It is our view that Crown agencies should have sufficient knowledgeable resources available to ensure the accounting standards are appropriately followed and consistently applied.

5.17 Some of the accounting concerns noted in Exhibit 5.2 related to issues observed during our audits, that required our Office's time to address or resolve prior to issuing our audit opinion. The occurrence of the annual financial statement audit does not fulfil the Board or management's responsibility to ensure adequate financial accounting expertise has been applied in the Crown agency's financial reporting.

Lack of segregation of duties

5.18 This year, we observed five Crown agencies where we had concerns regarding proper segregation of duties. Of these five Crown agencies, four also had a segregation of duties finding in our 2015 or 2014 Reports. We are pleased to note four Crown agencies (CCNB, NBCC, RDC, LA) had improvements in this area compared to our past findings.

5.19 Proper segregation of duties ensures the preparer and reviewer functions are performed by different people to eliminate the possibility of accounting work not being reviewed or being reviewed by the person who prepared it. Sometimes this also involves ensuring an appropriate segregation of duties in the accounting software or ensuring appropriate policies are in place to separate preparer and approval roles. Proper segregation of duties is also important to prevent loss or misappropriation of assets or occurrences of fraud or error.

5.20 When we note a lack of segregation of duties, our auditors normally perform extra procedures to reduce the risk of fraud or error in the financial statements. We encourage Crown agencies to review their financial processes to ensure these processes are properly structured and appropriate approval processes are present.

***Oversight/
governance
concerns***

5.21 Given recent Crown agency reorganizations, we encourage Crown agencies to be alert to potential segregation of duties concerns during agency restructurings or staff reorganizations. Safeguards should be in place so that separation of key accounting duties is maintained before and after any reorganization/restructuring activity.

5.22 There were six Crown agencies noted in our audits where we had concerns regarding oversight or governance processes. These concerns varied by entity and included items such as: lack of regular board meetings, lack of oversight of key decisions, delays in publishing annual reports, lack of risk management or internal control oversight, weaknesses in conflict of interest disclosures and other oversight/governance weaknesses.

5.23 We noted five of these Crown agencies also had oversight/governance concerns reported in either of our 2015 or 2014 Reports. We were pleased to note two Crown agencies (CCNB, LA) with improvements regarding their governance/oversight processes.

5.24 Effective oversight or "tone at the top", as well as Board commitment to transparency and public accountability, are important to building a strong internal control and risk management foundation for any Crown agency. We encourage Crown agencies to address governance or oversight findings provided to them during our audit.

***Accounting/
documentation
concerns with
estimates***

5.25 We noted concerns with the accounting and documentation process for estimates in four Crown agency financial statement audits. Of these four, two had an issue noted in either of our 2015 or 2014 Reports regarding estimates.

5.26 In three of the four Crown agencies where we noted concerns this year, the primary aspect of concern related to estimates supporting receivables balances (either accounts receivable or loans receivable), however, concerns regarding estimates were also noted for significant tangible capital asset values. We are pleased to note three Crown agencies (CCNB, NBAIC, NBCC) had improvement regarding estimate processes.

5.27 Estimates involve applying judgment to quantify unknown or uncertain amounts. Current auditing standards require that we examine estimates with more rigor, including reviewing the estimate's accuracy by comparing the estimate to current known outcomes and past accuracy history. This

is an important process to ensure estimates are as accurate as possible.

Management of agreements or third party arrangements

5.28 In our audits, we also noted a lack of appropriate support for management estimates. Management should document and support significant estimates used in preparing the financial statements. Support for significant estimates should also be reviewed by a second person other than the preparer.

5.29 We noted concerns with oversight and management of agreements or third party arrangements in four Crown agencies. Of these four, three were reported as concerns in either our 2015 or 2014 Reports.

5.30 Specifically, we noted in both provincial community colleges concerns regarding agreements with the Province. Key aspects of the operating arrangements such as accounting for improvements to buildings have not been clearly documented.

5.31 While we have observed satisfactory information to form our audit opinion, the colleges and the Province need to document these arrangements to ensure a common, clear understanding and to provide enhanced support for the current accounting treatment. Although progress on this matter has been made since we reported this finding in the prior two years, the issues are not yet addressed and resolved.

5.32 We noted one Crown agency (NBLGC) where improvement was noted regarding management of agreement or third party arrangements.

5.33 Our concern regarding management of agreements or third party arrangements may also be present for other Crown agencies we do not audit. We encourage all Crown agencies to ensure there is a clearly documented understanding of the responsibilities/rights/obligations to support significant accounting decisions contained in the Crown agency financial statements.

Financial Management/Cash Concerns

5.34 We noted concerns with financial management/cash in eight Crown agencies. As there were a number of similar findings, we identified this as a new audit findings theme this year.

5.35 The concerns noted include:

- insufficient management of inventory and proper inventory ordering quantity;

- delays in implementing investment policies;
- lack of approval of budgets used for comparison purposes in the audited financial statements;
- payment of duplicate invoices;
- a violation of the *Financial Administration Act* (in terms of obtaining appropriate spending approvals where budgets are overspent); and
- a lack of proper procedures for safe guarding of cash.

5.36 We are concerned at the nature of these findings as they directly relate to potential loss of assets, expending of public resources and appropriate asset management. They also indicate a greater level of due care is required with public resources to ensure assets are appropriately managed and protected and that proper budgeting practices and approvals are respected. We encourage all Crown agency boards of directors and management to ensure appropriate financial management/cash processes are operating effectively in each of their Crown agencies.

Applicability to other Crown agencies

5.37 We note a number of these themes from Crown agency audits have occurred in our prior years Reports. We encourage management of all Crown agencies to review these highlights and themes to consider if further improvements or adjustments are needed in their own organizations.

SNB Amalgamation

5.38 We noted in our audit of SNB that the Corporation is operating three separate financial reporting systems and three separate payroll systems. This structure presents significant risk of error or duplication and creates numerous inefficiencies when processing transactions and preparing financial reports.

5.39 While work on a new system is underway, we understand it could be three to five years before a solution is implemented. We are troubled at the ongoing exposure to risk of error, duplication and general inefficiencies over this time period. Further, we are very concerned it will be difficult for the amalgamated corporation to achieve significant synergies until such internal changes are made.

5.40 We have recommended SNB proceed as quickly as possible in implementing new accounting and payroll

systems. If an extended timeframe for completing these projects is expected, the Corporation should consider combining systems and transactions into one system in the short term.

Significant concerns regarding NBLGC

5.41 In our financial statement audit of NBLGC, we noted several significant concerns. Due to the large number of issues, we have described our findings in a separate chapter published in Volume III of our 2015 Report (Chapter 5).

5.42 We further note NBLGC's ongoing lateness in completion of the normal year end accounting and auditing exercise. At the time of writing, in autumn 2016, the last fiscal year audited for NBLGC was March 31, 2014. We find this ongoing delay extremely unusual and unacceptable given NBLGC's public reporting responsibilities.

Importance of timely completion of financial audits and public reporting

5.43 Producing financial statements with such a delay after the fiscal year end is still necessary, but the exercise holds much less value to the public and other users of this information if the reporting is not performed in a more timely manner. We strongly encourage all Crown agencies to promptly complete their financial reporting obligations.

Conclusion

5.44 While we have not noted any significant fraud, theft or error, the existence of the findings noted in Exhibit 5.2, increases the risk of loss or mistake in agencies' financial reporting. We encourage Crown agencies to address our findings prior to the next audit cycle.

Appendix I - Audit Objectives

5.45 Our examination of the matters included in this chapter of our Report was performed in accordance with Canadian generally accepted auditing standards, including such tests and other procedures as we considered necessary in the circumstances. The matters reported should not be used as a basis for drawing conclusions as to compliance or non-compliance with respect to matters not reported.

5.46 We obtain reasonable assurance on the financial statement figures because it would not be cost effective to obtain absolute assurance - our auditors cannot test every transaction.

5.47 By applying audit procedures to test the accuracy or reasonableness of the figures appearing in the financial statements, we achieve our desired level of assurance. We use audit procedures such as tracing samples of transactions to supporting documents, examining the effectiveness of certain internal controls, confirming year-end balances with third parties and reviewing the reasonableness of estimates.

5.48 Because of the limited objectives of this type of audit work, it may not identify matters which might come to light during a more extensive or special examination. However, it often reveals deficiencies or lines of enquiry which we might choose to pursue in future audit work.

Responsibilities of Crown Agencies

5.49 The Crown agencies are responsible for the preparation and the content of the financial statements or claims in accordance with the applicable accounting framework. When preparing the financial statements or claims, significant estimates may be made by the auditee, as not all information is available or determinable at the time of finalizing the statements.

Responsibilities of the Auditor General of New Brunswick

5.50 Our Office is responsible for auditing the financial statements or claims listed in paragraphs 5.2 and 5.3. An audit provides reasonable, but not absolute, assurance that the financial statement(s) or claim(s) are free of material misstatement or are in compliance with the relevant agreement. Material misstatement refers to an item or group of items that, if omitted or misstated, would alter the decisions of reasonably knowledgeable financial statement users. The tolerable level of error or misstatement is a matter of judgment.