

Chapter 3

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 2017

- 3.1** On August 22, 2017 the Auditor General signed an unqualified audit opinion on the consolidated financial statements of the Province of New Brunswick for the year ended March 31, 2017.
- 3.2** The opinion indicates the Province's consolidated financial statements are presented in accordance with Public Sector Accounting Standards. We are very pleased to be able to issue an unqualified audit opinion this year.
- 3.3** 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 and Crown agencies. 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

- 3.4** In almost every audit, there are audit findings to be discussed with management. The findings from our March 31, 2017 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 are presented in a letter to the provincial Comptroller. They are also summarized in a report to the Province's audit committee. We have selected the most important of our significant findings to be highlighted in this chapter.
- 3.5** 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.

3.6 We had several findings from the March 31, 2017 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.

Significant Findings During the Year

3.7 Highlights of our significant audit findings are presented in Exhibit 3.1. Overall, we are pleased at the number of prior year audit recommendations being implemented in 2017. We hope all remaining audit findings are corrected in advance of the next year's audit cycle

Exhibit 3.1 - Highlights and Recurring Themes

Theme	Finding	Finding addressed to	Concern in this area noted for 2017 AG Report	Concern in this area also noted for 2016 AG Report	Concern in this area also noted for 2015 AG Report	Paragraph Number
Accounting Concerns	Presentation of Pension Information	OOC ¹	Yes	Yes	No	3.44
	Unsigned Service Level Agreements with Vestcor	OCHRO ²	Yes	No	No	3.45
	Timely Completion of Crown Corporations and other Government Entity Audits	OOC ³	Yes	Yes	Yes	3.46
	NB Power Classification as a Government Business Enterprise	OOC ¹	Yes	No	No	3.47

Shaded findings indicate a concern in this area was also noted in the 2016 or 2015 AG Reports

¹Office of the Comptroller, Department of Treasury Board

²Treasury Board – Office of the Chief Human Resources Officer

³Findings not addressed to OOC prior to 2017

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

3.9 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 3.1 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**

3.10 Our detailed observations, recommendations and departmental responses to the significant findings highlighted in this chapter are presented in Appendix III.

**Additional
Discussion**

3.11 During our 2017 audit of the Province's consolidated financial statements, we noted significant accounting concerns. We also had findings related to accounting concerns in our 2016 and 2015 Annual Reports.

**Accounting
concerns**

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

3.13 The theme of accounting concerns was notably the area where we saw the greatest implementation of our prior year audit recommendations including: presentation of budget numbers, accounting for school raised funds and netting of assets and liabilities.

3.14 Prior year accounting concerns continue in the areas of presentation of pension information and timely completion of Crown Corporations and other government entity audits (as reported in our prior years' Crown agencies chapter). Also, new in 2017, we had audit findings in areas such as: unsigned service level agreements with Vestcor and NB Power classification as a government business enterprise. Given the significance of these findings, we hope they are addressed before the next audit.

Information Technology Findings

Auditing the Province's systems and information technology

3.15 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 3.2 lists IT systems we examined in the past year.

Exhibit 3.2 - 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

*** - Work on this system was performed during our special examination of property assessments. Our findings are reported in Volume III Chapter 2.

Key themes

3.16 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 3.3.

Exhibit 3.3 - 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)
Segregation of duties	Property tax system	Finance (Ptax)
	Access to supplier information	SNB (IPM)
	Review of summer pay accrual	EECD
IT security	Excessive permissions	OOO (Oracle), SNB (IPM) Finance (Ptax)
	Disabling access	SNB (IT Infrastructure), SNB (IPM)
	Account management	SNB (IPM)
	Security of data	SNB (IPM)
	Monitoring – Super user access	SNB (HRIS)
	Management of network access	SNB (IT Infrastructure)
Data integrity/accuracy/ completeness	Quality of sick leave data	EECD
Non-compliance with policies/standards/guidelines	Annual client reviews	SD (NBFamilies)
Other observations from our IT work	Business continuity/disaster recovery plan	SNB (HRIS), OOC (Oracle)

3.17 We are not aware of any significant loss of government assets or errors which resulted from the findings noted in Exhibit 3.3, 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 3.3 we are also concerned for the potential of loss of confidentiality and privacy inherent in the findings if they remain uncorrected.

3.18 Of particular interest again this year is the number of IT systems needing replacing or modernizing. We continue to be concerned about the timeline for replacing these older systems. We understand all three of these outdated systems will be replaced with a new enterprise-wide system for government which will encompass the procurement/supply chain, human resource, financial resource and customer relationship management. We will continue to monitor and report on the progress of the system implementation in

future reports.

3.19 It should be noted, our 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

3.20 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, the SNB (HRIS) payroll system will no longer be supported after 2017 and the IPM system (which is used to enter vendor invoices for payment) is no longer fully supported by the supplier. We did note SNB has developed alternative procedures for processing payments should the IPM system fail.

3.21 As mentioned in paragraph 3.18, all three of these systems will be replaced by one new government-wide system which SNB and Treasury Board have joint responsibility for procurement. The project is now in the middle of the procurement process. A request for proposal was issued in September and the project team is in the process of evaluating the responses.

3.22 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, outdated hardware. The system is over 20 years old and is at risk of failure. This year we recommended the EECD update its risk assessments for this system and in particular develop monitoring procedures to prevent/detect fraud in payroll.

Segregation of duties

3.23 This year we had three findings relating to segregation of duties. Maintaining proper segregation of duties helps to reduce the risk of fraud and/or error in financial processes and is necessary for a strong control environment. While our three findings were all different in nature, they ultimately result in risks for the organizations (Finance, SNB, EECD).

3.24 We found:

- banking information could be entered or changed without approval or review from another individual;

- system access allowed users to select and approve items for write-off ;
- roles and responsibilities that establish segregation of duties for a system have yet to be reviewed and approved; and
- information required for preparing significant financial estimates was not reviewed by a second individual.

IT security - Excessive permissions

3.25 We had two findings relating to excessive system access.

- For two systems, we found access to sensitive files such as payment files, images and audit trails 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 data manipulation or disclosure of potentially confidential information.
- For another system, we noted 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

3.26 We noted findings in two of our SNB audits relating to disabling system access. We found instances where users' access was not disabled in a timely manner, database accounts were not disabled when access was no longer required, and employees had system access that was no longer required to perform their job responsibilities.

3.27 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 – Account management

3.28 In our SNB (IPM) audit, we noted the passwords for two accounts, which were shared between two individuals, had not been changed since 2010. Not changing passwords on a regular basis increases the risk of fraud or error through unauthorized access to data. Sharing system accounts impacts accountability making it difficult to determine who is responsible for changes.

IT security - Monitoring super user access

3.29 In our SNB HRIS audit, we found an issue with the approval and monitoring of the super user account. Super user accounts have powerful system access and require proper monitoring controls to reduce the risk of

unauthorized changes or updates to the system and data.

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

3.30 In our EECD audit, we had one finding relating to the integrity, accuracy and completeness of data. The finding related to the quality of sick leave data for teachers. We found errors in the information provided to actuaries which is used to estimate the sick leave liability for the Province. Providing inaccurate information to the actuaries affects the precision of the estimate which ultimately affects the financial results of the Province.

***Non-compliance with
policies/standards
/guidelines***

3.31 In our SD (NBFamilies) work, we found three cases in 15 items tested where clients' annual case reviews were not up-to-date as required by departmental guidelines. Regular case reviews and client contact helps reduce the risk of clients receiving inappropriate levels of care to meet their needs.

***Other observations –
Disaster recovery and
business continuity
planning***

3.32 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.

Appendix I - Audit Objectives

3.33 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.

3.34 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.

3.35 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.

3.36 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

3.37 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).

3.38 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

3.39 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.

3.40 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 Energy and Resource Development Missing equipment from various regions	\$ 6,950
Department of Education and Early Childhood Development Missing equipment	\$ 3,883
Department of Transportation and Infrastructure Missing equipment	\$ 16,154
Department of Tourism, Heritage and Culture Missing equipment	\$ 3,500
Department of Justice and Public Safety Missing cash and equipment	\$ 3,054
Department of Environment and Local Government Missing equipment	\$ 140
Department of Post-Secondary Education, Training & Labour Missing cash	\$ 125

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

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

3.43 In 2017, the Province reported lost tangible public assets in the amount of \$33,806 compared to a loss of \$259,700 reported for 2016.

Appendix III - Significant Findings

3.44	Presentation of Pension Information	
<p>We again noted detailed information for \$13 billion in pension plans was not included on a plan by plan basis in the Province's financial statements. It had been past practice to include this information in the notes to the Province's financial statements in 2014 and prior years even though it was not required by Canadian public sector accounting standards (PSAS). We believe the pension information, as well as information for retirement allowances, should be included each and every year on a plan by plan basis to provide more detailed and transparent information to readers of the Province's financial statements. We note at the Audit Committee meeting on August 17, 2017 OOC has agreed to make these disclosures next year.</p>		
Recommendation		Comments from Management
<p>We recommend the Office of the Comptroller disclose on a plan-by-plan basis, pension and retirement allowance information in the financial statements.</p>		<p><i>On a go forward basis, the Office of the Comptroller has committed to disclosing pension and retirement allowance information on a plan by plan basis in the consolidated financial statements.</i></p>
<p>Timeline for Implementation: <i>Implemented by March 31, 2018</i></p>		

3.45	Unsigned Service Level Agreements with Vestcor	
<p>We noted the Treasury Board – Office of the Human Resources Officer (OCHRO) did not have signed service level agreements with Vestcor (the plan administrator of the Province's employee benefit programs) for the day-to-day administration services for certain provincially governed employee benefit programs. Without signed agreements with Vestcor, the Province is exposed to risk that it may not agree with charges or the services provided.</p>		
Recommendation	Comments from Management	
<p>We recommend the Treasury Board – Office of the Human Resources Officer sign service level agreements with Vestcor for the administration of the Province's employee benefit programs.</p>	<p><i>There is representation from Treasury Board on the Governing Committees for the Employee Benefit Programs and Pension Plans. The Governing Committees are responsible for the plan budget, monitoring and oversight of plan administration costs, KPI's, service standards, and risk management.</i></p> <p><i>Treasury Board is currently working on two service level agreements (SLA); one for the plan administration of employee benefits and one for the plan administration of government sponsored pension plans.</i></p>	
<p>Timeline for Implementation: <i>Implemented by March 31, 2018</i></p>		

3.46	Timely Completion of Crown Corporations and Other Government Entity Audits	
<p>Consolidation is the process of combining all the financial statements of Crown corporations and other government entities ('components') into the financial statements of the Government Reporting Entity (GRE). As the auditor of the GRE, we are required to assess the work of external component auditors in order to support our audit work.</p> <p>In our selection of component auditors to review for the 2017 audit, we noted three instances where audits were either not started, or completed at the end of July, the end of our fieldwork. We also noted for other component auditors selected, we were unable to review the audit files until late in our audit fieldwork.</p> <p>To satisfy audit requirements, we performed alternate procedures by auditing significant balances and transactions, and adjusted our internal timelines in order to meet audit deadlines as agreed with the Office of Comptroller. It is essential we review component auditor files in a timelier manner in future periods to ensure these deadlines are respected.</p>		
Recommendations		Comments from Management
<p>We recommend the Office of the Comptroller communicate strict audit completion deadlines to Crown corporations and other government entities in advance of next year's audit.</p>		<p><i>The Office of the Comptroller will communicate audit completion deadlines to crown corporations and other government entities in advance of next year's audit.</i></p>
<p>Timeline for Implementation: <i>Implemented by March 31, 2018</i></p>		

3.47	NB Power Classification as a Government Business Enterprise	
<p>NB Power is classified as a Government Business Enterprise (GBE) within the Government Reporting Entity (GRE). This requires the Province to record its investment in NB Power using the modified equity method – a method that does not combine all balances into the GRE. In order to continue this classification, NB Power must meet certain accounting criteria, including the ability to self-sustain its operations without assistance from the Province.</p> <p>In recent years, NB Power’s ability to self-sustain its operations has been called into question as:</p> <ul style="list-style-type: none"> • There is a \$1 billion deferred regulatory asset for the Pt. LePreau refurbishment which is supported by a forecasted reasonability model (which is not being fully realized as expected); • While debt is slowly decreasing, net earnings (2017- \$27M, 2016 - \$12M) continue to be nominal for an entity with a significant debt burden (2017 – \$4.9B, 2016 - \$4.2B); and • Significant expenditures are expected in the future for the refurbishment of the Mactaquac dam, which will put burden on cash flow. <p>During our audit, we performed an assessment to confirm the entity continues to meet accounting criteria, and thus can continue its classification as a GBE. However, this assessment should be prepared by the Office of the Comptroller annually, in coordination with NB Power.</p>		
<p>Recommendation</p> <p>We recommend the Office of the Comptroller perform an accounting assessment of NB Power’s classification as a Government Business Enterprise on an annual basis. This assessment should be retained for audit purposes, and be available in advance of next year’s audit. The analysis should include a discussion of accounting criteria, and updated model calculations for the reasonability model on an annual basis to ensure the deferred regulatory asset remains collectible.</p>	<p>Comments from Management</p> <p><i>The Office of the Comptroller will perform the accounting assessment in accordance with the recommendation.</i></p>	
<p>Timeline for Implementation: <i>Implemented by March 31, 2018</i></p>		