
Reflections of the Auditor General



The following comments are made further to my audit of the Public Accounts of the Province for the year ended 31 March 2004. The Report provides additional information on the financial condition of Government measured by using indicators issued by the Canadian Institute of Chartered Accountants. The Report also offers comments on Government's compliance with generally accepted accounting principles and adherence to principles of sound financial accountability.

Financial Condition of Government

The annual surplus or deficit shows the extent to which a government spends less or more than it raises in revenues in one fiscal year - it shows if a government is living within its means. The accumulated deficit or surplus is the sum of all annual deficits and surpluses. In the Public Accounts, the net debt is the total of all liabilities (e.g. borrowings, group health and life insurance retirement benefits, unfunded pension liability) less financial assets (e.g. cash and accounts receivable).

For the year ended 31 March 2004 I report that Government did not spend within its means. The deficit for 2004 was \$913.6 million, the largest deficit ever reported by the Province. This has been an annual recurring theme of our Province's fiscal performance. In fact, with the exception of 1998, Government has had an annual deficit every year since 1994, the first year consolidated summary financial statements were prepared. These deficits will eventually have to be either paid or refinanced.

The net debt at 31 March 2004 was \$11.5 billion. On a per capita basis this amounts to approximately \$22,200 for each Newfoundlander and Labradorian. This per capita net debt is the highest of any province in Canada. Although the Province's gross domestic product (GDP) has been increasing, our net debt has also been increasing. In 2004, the net debt as a percentage of GDP was 63.7% - the highest net debt as a percentage of GDP of any province in Canada.

Interest costs in 2004 amounted to \$1.1 billion and represented 25.4% of total revenue in that year - the highest interest costs as a percentage of total revenue of any province in Canada. This "interest bite" means fewer resources to allocate to programs and services.

It is encouraging that Government has indicated its commitment to address the Province's annual deficits and net debt. I will, on behalf of all Members of the House of Assembly, continue to monitor Government's fiscal performance and report annually as to whether progress is being made to bring the Province's finances in order.

Retirement Benefits - Pensions (Part 5.1)

At 31 March 2004 the unfunded pension liability totalled \$3.75 billion and continues to be a significant issue for Government. The unfunded pension liability increased by \$188.7 million during the year, a 5.3% increase from the \$3.56 billion balance at 31 March 2003. Since 1994, the unfunded pension liability has increased by \$1.23 billion or 49%.

In 1998, in an attempt to address the unfunded pension liability, Government started to make special payments into the pension fund. Since 1998 Government has made special payments totalling \$1 billion. However, these special payments are not large enough to reduce the unfunded pension liability - in fact the unfunded liability continues to grow. To put this into perspective, for the year ended 31 March 2004 Government made a special payment of \$163.5 million to the pension fund; however, even with this significant special payment the unfunded pension liability increased by \$188.7 million. Interest costs alone on the unfunded pension liability during the year amounted to \$330.9 million (i.e. \$167.4 million more than the special payment made by Government in an attempt to address the unfunded pension liability).

Addressing the unfunded pension liability should remain a priority for Government.

Retirement Benefits - Other Than Pensions (Part 5.2)

Government provides retirees with group health and group life insurance benefits. At 31 March 2004 the Province's net liability for these retirement benefits was \$1.058 billion. This liability has added to the already considerable debt load of the Province and, if action is not taken to address it, is expected to increase in each of the next five years. By 2009 the liability is expected to total \$1.552 billion, an increase of \$567 million or 58% over the \$985 million liability for 2003.

Government should carefully manage its liability relating to group health and group life insurance benefits.

Accounts Receivable (Part 5.4)

Government has historically focused on expenditures and not revenues. The lack of focus on revenues is a contributing factor in why Government does not do a good job in collecting amounts owed to it and, therefore, a significant portion of its receivables have either been written off or are considered doubtful of collection. At 31 March 2004 Government departments were owed \$501 million of which \$185 million (36.9%) has been outstanding in excess of one year and \$243 million (48.5%) is considered to be uncollectible. In addition, since 1992, Government has written off a total of \$268 million in accounts receivable.

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Although Treasury Board indicated in 2002 that initiatives would be undertaken in an effort to improve collection of accounts receivable, the initiatives are still not in place. The Department of Finance was to establish a Central Provincial Collector function to provide assistance and training to departments in their collection efforts; however, this is still not in place. The Department of Finance was also to reinstate action to seek approval for Provincial participation in the Federal set-off program; however, although approval has been obtained, the program is still not in place. In addition, Treasury Board directed departments to document policies and procedures relating to the collection of accounts receivable; however, many departments have not yet documented their accounts receivable procedures.

Collecting monies owed on a timely basis is especially important given that the Province is reporting record annual deficits and debt.

Government should be more diligent in collecting amounts owed to it and ensure that the initiatives identified by Treasury Board to improve collection of accounts receivable are implemented.

Government Reporting Entity (Part 3.2)

The Province's Consolidated Summary Financial Statements are required to include all organizations that are controlled by Government. However, Government does not include Memorial University of Newfoundland in these statements. My Office has been recommending the inclusion of the University since 1994 when the Consolidated Summary Financial Statements were first prepared. Some jurisdictions believed the criteria, issued by the Public Sector Accounting Board (PSAB) of the Canadian Institute of Chartered Accountants to determine whether an entity should be included, lacked clarity. Therefore, PSAB undertook a project to clarify the criteria and in August 2003 issued new rules. Again, the University meets the criteria for inclusion. Government is required to follow these new standards for fiscal years beginning 1 April 2005 (i.e. 2005-06 fiscal year).

For the year ended 31 March 2004, the University reported revenues of \$322.6 million, expenditures of \$347.4 million and had assets totalling \$264.3 million - it is a material entity and should be included in the Province's Consolidated Summary Financial Statements. Therefore, if the standards do not change and Memorial University of Newfoundland is not included in the Province's Consolidated Summary Financial Statements for 2005-06, I will have no alternative other than to qualify my auditor's opinion and state that the Province's financial statements are not complete.

Government should include Memorial University of Newfoundland in the Province's Consolidated Summary Financial Statements.

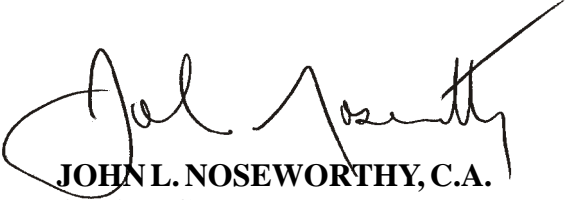
Environmental Liabilities (Part 3.3)

In my 2002 Annual Report to the House of Assembly I concluded that *"There is no central inventory of contaminated sites ... The lack of a central inventory makes it more difficult for Government to determine the nature and extent of contaminated sites in the Province, the extent of progress of remediation efforts, and estimated future remediation costs to be incurred by Government."*

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There is still no complete central inventory of contaminated sites and there is no liability recorded on the Province's financial statements for remediation costs associated with these sites. The only information currently noted in the financial statements is found in Note 9 (c) (vi) which states that "... *the status and costs of potential [environmental] issues are not determinable*". I note that a report made public by Government in January 2004 referred to an estimated cost of \$237 million relating to the remediation of contaminated sites.

Government should undertake a process to identify all contaminated sites in the Province for which it is potentially liable, determine its share of remediation costs and record any resulting liability in the Province's financial statements.



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