Figure 1

Consolidated Summary Financial Statements
Key Balances
Years Ended 31 March
($ Billions)

Balance	2004	2005	2006
Statement of Financial Position			
Financial Assets	1.399	1.845	2.118
Liabilities	12.886	13.733	13.802
Net Debt	**11.487**	**11.888**	**11.684**
Non-Financial Assets	2.176	2.135	2.289
Accumulated Deficit	**9.311**	**9.753**	**9.395**
Statement of Operations			
Revenue	4.219	4.483	5.556
Expense	5.133	4.972	5.357
Annual Surplus (Deficit)	**(.914)**	**(.489)**	**.199**

Source: Consolidated Summary Financial Statements

3.3 The Financial Condition of the Province

While Government's financial condition has improved somewhat, its net debt of $11.7 billion is still quite high, with net debt per capita of $22,924 as at 31 March 2006, still the highest in the country.

Also, while the Province's economic growth has been positive, its ability to raise its own source revenue remains vulnerable to changes in the economy, including changes due to fluctuations in oil prices and production levels, the Canadian dollar and interest rates.

With regards to oil revenues, the Province is becoming increasingly reliant on these revenues due to growth in this revenue source in recent years. Actual oil revenue in 2004 was $127 million and increased by $406 million to $533 million in 2006. These revenues are generated from non-renewable resources and are very vulnerable to changes in world oil prices and production levels - both outside the control of Government. As a result, there can be significant variances between Government estimated revenue and actual revenue which can have significant impacts on fiscal performance. To illustrate, in November 2006, Government decreased its oil revenue estimate for the 2007 fiscal year by $206.7 million due to production levels being lower than expected. This had a significant impact on the expected fiscal outlook and was a major factor in changing the projected surplus of $6.2 million to a projected deficit of $39.8 million for the 2007 fiscal year.

Government has committed to addressing past annual deficits, and for 2006 reported a surplus of $199 million. However, it is important that Government continue with efforts to spend within its means and consider a reasonable plan to reduce the Province's substantial net debt of $11.7 billion.

In order for Government to eliminate or reduce its net debt, it will be necessary to have continued annual surpluses. The Province has had an annual deficit each year from 1995, with the exception of 1998 and 2006, and is projecting a deficit for 2007. There has to be a substantial improvement in Government's results of operations in order to support a reasonable plan to address the substantial net debt. By way of illustration, consider that the Province would require a surplus of nearly $300 million each year for almost 40 years to eliminate its current net debt of $11.7 billion.

Maintaining a significant net debt means incurring significant annual costs to service that debt. It also means that these annual costs could change significantly due to changes in interest rates. Debt expenses for the year ended 31 March 2006 totalled $947 million, which represents 17% of total revenues. This means that the Province spent $947 million to pay financing costs associated with past accumulated deficits and, as a result, that amount was not available to spend on programs and services. Furthermore, the Province currently has $1.0 billion in U.S. debt (net of sinking fund assets) and therefore has exposure to currency fluctuations. For example, a 1 cent change in the Canadian dollar has an impact of $11.5 million on the Province's debt.

The Province is also heavily reliant on transfers from the Federal government in order to fund its programs and services. To illustrate, of the Province's total revenue of $5.6 billion for the year ended 31 March 2006, $1.9 billion or 34% resulted from Federal transfers, including $861 million for equalization.

Aside from the risk of fluctuating revenues, Government faces continued demand for expenditures, especially in health and education. Expenses in these two departments over the last five years increased by $1.0 billion (or 50%) from $2.0 billion for 2001 to $3.0 billion for 2006, and accounted for 57% of total Government expenses for the year ended 31 March 2006.

There are other factors which could also result in changes to the annual surplus or deficit including an aging infrastructure, an aging population and out-migration.

Figure 2 provides details of the Province's liabilities, annual surplus (deficit), net debt and debt expenses for the years 1995 to 2006 as reported in the consolidated summary financial statements of the Province.

Figure 2

Consolidated Summary Financial Statements
Liabilities, Annual Surplus (Deficit), Net Debt and Debt Expenses
Years Ended 31 March
($ Millions)

Year	Net Borrowing and other Liabilities	Unfunded Pension Liability	Group Health and Group Life Insurance Benefits Liability	Total Liabilities	Annual Surplus (Deficit)	Net Debt	Debt Expenses
1995	6,535	2,686		9,221	(374)	6,831	1,004
1996	6,725	2,739		9,464	(190)	7,121	822
1997	6,730	2,943		9,673	(107)	7,254	819
1998	6,373	3,134		9,507	133	7,301	865
1999	6,758	3,352		10,110	(187)	7,851	1,008
2000	6,689	3,309		9,998	(269)	8,087	883
2001	6,801	3,348		10,149	(350)	8,437	951
2002	7,270	3,392		10,662	(468)	8,932	942
2003	7,581	3,557	985	12,123	(644)	10,616	979
2004	8,073	3,746	1,067	12,886	(914)	11,487	982
2005	8,640	3,934	1,159	13,733	(489)	11,888	940
2006	10,336*	2,201	1,265	13,802	199	11,684	947
Total					**(3,660)**		**11,142**

* Includes deferral of $1.678 billion Atlantic Accord (2005) money

As Figure 2 shows, the Province has had substantial deficits and interest costs and an increasing net debt each year, with the exception of a slight decrease in 2006. The total deficit reported over the 12 year period is $3.660 billion, with total debt expenses over the same period of $11.142 billion.

Although for 2006 the Province had budgeted a deficit of $492 million, it actually had a surplus of $199 million. Figure 3 provides details on the budget forecast compared to actual results for the year ended 31 March 2006.

Figure 3

Consolidated Summary Financial Statements
Actual Compared to Budget
31 March 2006
($ 000's)

	Actual	Original Estimates	Impact on Deficit	% of Impact
Revenue				
Provincial				
Taxation	2,111,056	1,991,868	(119,188)	17.2%
Investment	296,992	278,117	(18,875)	2.7%
Fees and fines	231,179	160,438	(70,741)	10.2%
Offshore royalties	532,533	215,370	(317,163)	45.9%
Other	325,794	270,249	(55,545)	8.0%
Government of Canada	1,880,002	1,748,358	(131,644)	19.0%
Net income of government business enterprises	178,032	174,403	(3,629)	0.5%
Total Revenue	**5,555,588**	**4,838,803**	**(716,785)**	**103.5%**
Expense				
General Government Sector	1,494,843	1,519,430	(24,587)	3.6%
Resource Sector	184,546	199,688	(15,142)	2.2%
Social Sector	3,676,917	3,612,149	64,768	-9.3%
Total Expense	**5,356,306**	**5,331,267**	**25,039**	**-3.5%**
Surplus (Deficit)	**199,282**	**(492,464)**	**(691,746)**	**100.0%**

Figure 3 highlights the impact that fluctuations in oil revenue and Federal government transfers have on the Province's surplus or deficit. As the Figure shows, the significant increases in oil revenue ($317 million) and Government of Canada revenue ($132 million), were major factors in why the projected deficit of $492 million became an actual surplus of $199 million.

There is a sense of optimism about the potential prosperity for the Province and the resulting improvements to the Province's financial condition. The most significant area relates to the receipt of the $2 billion advance payment from the Government of Canada in July 2005 relating to the Atlantic Accord (2005), and the future revenues to be recognized resulting from this advance payment along with reductions in pension debt expenses. Another notable area is the continuing increase in oil revenues. These have had an immediate impact on the Province's financial position and are expected to have a significant impact on the Province's results of future operations. However, it has to be recognized that oil revenues are volatile and oil is a non-renewable resource with a limited life.

While it is encouraging that Government has made some progress regarding past annual deficits, prudent fiscal management and spending within its means has to remain a priority for Government if it is to make progress in improving the Province's financial position. As well, a debt reduction plan has to be developed and followed before the financial condition of the Province can be considered to have turned around.

3.4 Financial Indicators - Interpreting the Financial Information

An important role for my Office is to provide Members of the House of Assembly with information on the state of Government's finances. This information is necessary in order to have an informed debate about the issues that Government has to address. Issues include the ability of Government to fund programs and services, where the revenues will come from and the impact of surpluses, deficits and debt.

The Canadian Institute of Chartered Accountants (CICA), through the Public Sector Accounting Board (PSAB) is the professional body that approves standards for financial reporting and accounting in the public sector. It also issues research studies on public sector accounting matters.

CICA issued a Research Report in 1997 entitled Indicators of Government Financial Condition. That report identified financial indicators which it felt best describes the financial condition of a government. These indicators were categorized in terms of three elements of financial condition: