Finance

10

Main points

In this chapter, we report the results of the audit of the Department of Finance (Finance) and the entities it controls.

The General Revenue Fund's (GRF) 2003 financial statements are not reliable. They do not record the GRF's pension liability of $4 billion, and they understate the year's pension costs by $24 million. The statements also inappropriately record an $82 million transfer to the Fiscal Stabilization Fund as an expenditure and $58 million as loans receivable from Crown corporations. As a result, Finance's accounting practices are not in accordance with generally accepted accounting principles for the public sector.

We have significant concerns with the GRF financial statements because the Government uses the GRF's annual surplus or deficit as one of its key performance indicators. In March 2003, the Government announced it would present a summary financial plan for the entire Government as part of the 2004-05 budget package. We are hopeful that the Government will report on its performance using this summary financial plan together with its summary financial statements, rather than using the GRF statements.

Finance did not comply with the reporting required by *The Balanced Budget Act*. Finance should have prepared the annual update report using accounting policies in place at the start of the four-year plan. Instead, beginning in 2003, Finance used different accounting policies for education capital projects to prepare the annual update report. As a result, in the annual update report, operating spending is understated and the cumulative surplus is overstated. In addition, the current balanced budget legislation only focuses on balancing the financial results of the GRF. If it is Government policy to have balanced budget legislation, the Government should consider legislation based on balancing the financial results of the entire Government.

Introduction

The Department of Finance (Finance) helps the Government and the Legislative Assembly manage and account for public money. It controls spending from the General Revenue Fund (GRF) and ensures that the GRF receives all revenue due to it. In addition, Finance prepares the Government's summary financial statements.

Finance:

- prepares the annual Budget Address, Estimates, and Public Accounts;
- arranges Government financing, banking, investing, and borrowing;
- provides policy and financial analysis to Treasury Board and Executive Council;
- develops tax policy alternatives;
- administers various tax, grant, and refund programs;
- provides economic forecasting and economic, social, and statistical data;
- administers public sector pension and benefit plans; and
- leads the Government's accountability project.

In 2003, Finance spent $1.2 billion and collected revenue of $5.2 billion. Revenue includes $314 million of debt costs recovered from Crown agencies.

Special purpose funds and Crown agencies

Finance is responsible for the following special purpose funds and Crown agencies.

Year-end March 31

General Revenue Fund (GRF)
Fiscal Stabilization Fund[1]
Public Employees Benefits Agency Revolving Fund
Public Employees Pension Plan
Public Service Superannuation Plan
Saskatchewan Pension Annuity Fund
Extended Health Care Plan for Retired Employees
Extended Health Care Plan for Certain Other Retired Employees

Year-end December 31

Extended Health Care Plan
Extended Health Care Plan for Certain Other Employees
Municipal Employees' Pension Commission
Municipal Financing Corporation of Saskatchewan
Public Employees Deferred Salary Leave Fund
Public Employees Disability Income Fund
Public Employees Dental Fund
Public Employees Group Life Insurance Fund
Saskatchewan Pension Plan
SaskPen Properties Ltd.[2]
Saskatchewan Power Corporation Supplementary Superannuation Plan

[1] The Department does not prepare financial statements for this Fund. As required by *The Fiscal Stabilization Fund Act*, a schedule of transfers and accumulated balance appears in Public Accounts Volume 1.
[2] The Government denied us access to this Crown agency; therefore, we could not audit the agency (see Chapter 8 of our 1999 Fall Report-Volume 2 for further discussion of the matter).

Financial Overview

The following is a list of Finance's major programs and spending for the year ended March 31, 2003. The financial information is from the *Estimates 2002-2003, Public Accounts 2002-2003: Volume 1: Main Financial Statements* (to view a copy of this report, see http://www.gov.sk.ca/finance/paccts) and *Saskatchewan Finance's Annual Report 2002-2003*.

	Original Estimates	Actual
	(in millions of dollars)	
Interest - GRF debt	$ 633	$ 611
Interest - Crown corporation debt	314	314
Total interest on debt	$ 947	$ 925
Pensions and benefits	188	247 *
Administration	39	37
	$1,174	$1,209

*Adjusted by $61.5 million – see Pension Costs Reservation section.

The following is a list of Finance's major revenue sources:

	Original Estimates	Actual
	(in millions of dollars)	
Individual Income Tax	1,166	1,430
Interest - Crown corporations	314	314
Sales Tax	827	814
Transfers - CHST**	638	668
Transfers - Equalization	531	(9)
Fuel Taxes	358	332
Corporation Taxes	459	557
Tobacco Taxes	183	158
Income from Government Entities	686	672
Motor Vehicle Fees	117	117
Other	114	137
Total	5,393	5,190

** Canada Health & Social Transfer

Key risks

It is important that Members of the Legislative Assembly (MLAs) and the public know the key risks facing a department. Also, they should receive information on these risks to assess a department's performance. We think sharing our understanding with MLAs and the public will help them better assess Finance's performance.

Information on how Finance is managing its key risks can increase public confidence. Annual reports may provide this information to MLAs and the public. Finance prepares an annual report that includes important accountability information about its activities, goals, and challenges. We identified the following key risks Finance must manage well to be successful. It must:

- give Treasury Board accurate and useful information to enable it to develop, manage, and evaluate the Government's fiscal plan;
- publish useful planning and performance reports;
- manage the Government's debt;
- manage investments;
- collect revenues due to Finance;
- manage several government pension and benefit plans; and
- ensure designated government entities comply with Treasury Board's directives.

To identify these key risks, we reviewed *The Financial Administration Act, 1993* and other legislative authorities. We also reviewed the Estimates, the Public Accounts, the Budget Address, Finance's annual report, and prospectus documents. In addition, we discussed these issues with key officials.

Our audit conclusions and findings

This chapter contains our audit conclusions and findings on Finance, its special purpose funds, and its Crown agencies for the year ended March 31, 2003, the Municipal Employees' Pension Commission and the Municipal Financing Corporation of Saskatchewan for the year ended December 31, 2002.

Our Office worked with KPMG LLP, appointed auditor for the Public Employees' Pension Plan and the Municipal Employees' Pension Commission and E.J.C. Dudley & Co. for Municipal Financing Corporation of Saskatchewan. We used the framework recommended by the *Report of the Task Force on Roles, Responsibilities and Duties of Auditors* (to view a copy of this report; see our web site at http://www.auditor.sk.ca/rrd.html).

In our opinion:

- **the Government's summary financial statements, included in the Public Accounts 2002-2003 Volume 1 are reliable;**

- **the financial statements for the special purpose funds and Crown agencies listed above are reliable except for the GRF;**

- **the GRF's financial statements included in the Public Accounts 2002-2003 Volume 1 are reliable except that the transfer to the Fiscal Stabilization Fund, loans receivable from Crown corporations and all pension costs are not properly recorded;**

- **Finance, its special purpose funds, and its Crown agencies that we audited had adequate rules and procedures to safeguard public resources except for the matters reported in this chapter; and**

- **Finance, its special purpose funds, and its Crown agencies that we audited complied with authorities governing their activities relating to financial reporting, safeguarding public resources, revenue raising, spending, borrowing and investing except where we report otherwise in this chapter.**

In addition, the law requires us to report when a special warrant approved the payment of public money. For the year ended March 31, 2003, the Government approved the spending of $137.9 million by special warrant. It later included these special warrants in an appropriation act.

GRF financial statements

Our auditor's report on the GRF's financial statements for the year ended March 31, 2003 warns readers that the financial statements do not include all of the Government's financial activities. Therefore, readers should not use the GRF's statements to assess the Government's overall performance. The appropriate financial statements to use for that purpose are the Government's summary financial statements.

In addition, our auditor's report on the GRF's financial statements for the year ended March 31, 2003 includes three reservations. The financial statements are not reliable because they do not properly record transfers to the Fiscal Stabilization Fund, loans receivable from Crown corporations, and pension costs.

The combined effects of these three reservations are as follows:

- the transfer to the Fiscal Stabilization Fund of $82 million overstates expenditures by $82 million;
- transfers to Crown corporations, improperly recorded as loans, understate expenditures by $58 million;
- pension costs are understated by $24 million; and
- pension liabilities are understated by $4.0 billion, assets are understated by $0.5 billion, and accumulated deficit is understated by $3.5 billion.

As well, the financial information reported in Volume 2 of the Public Accounts 2002-03 and some department annual reports is not reliable because it is based on information reported in the GRF financial statements.

For the reservation related to transfers to Crown corporations improperly recorded as loans, *Saskatchewan Learning's Annual Report 2002-2003* understates K-12 Education School Capital expenditures by $7.1 million and Post-Secondary Capital expenditures by $30.9 million. *Saskatchewan Agriculture, Food, and Rural Revitalization's Annual*

Report 2002-2003 understates crop insurance expenditures by $20 million.

For the reservation related to pension expenditures, *Saskatchewan Learning's Annual Report 2002-2003* overstates expenditures by $37.5 million for the Teachers' Superannuation Plan. *Saskatchewan Finance's Annual Report 2002-2003* understates expenditures by $61.5 million for pension plans managed by the Public Service Superannuation Board.

Fiscal Stabilization Fund reservation

The Government records transactions between the GRF and the Fiscal Stabilization Fund (Fund) as GRF revenue or expenditure. The substance of the transactions between the GRF and the Fund is that amounts owed by the GRF to the Fund must be repaid to the GRF by the Fund. Canadian generally accepted accounting principles (GAAP) for the public sector do not allow the GRF to record changes in the amounts due to the Fund as revenues or expenditures of the GRF. The Government acknowledges that it does not follow GAAP for transfers to and from the Fund.

The GRF's 2003 financial statements show a liability of $577 million owed to the Fund, an increase of $82 million from 2002. This increase is recorded as a GRF expenditure. It is not appropriate to record the $82 million as an expenditure because the Fund must return it to the GRF. Instead of recording an expenditure of $82 million, the GRF should show an asset of $577 million owed from the Fund.

The effects of not reporting this asset properly are as follows:

- the GRF's expenditure is overstated by $82 million;
- the GRF's surplus is understated by $82 million;
- assets are understated by $577 million; and
- accumulated deficit is overstated by $577 million.

The Legislative Assembly created the Fund in April 2000. The Fund's stated purpose is to stabilize the fiscal position of the Government from year to year. However, making transfers from one fund to another, and back again, has no effect on the Government's overall annual surplus (deficit) and accumulated deficit. The Government's total accumulated deficit of $9.3 billion is unaffected. Therefore, the only consequence of recording these transactions in the GRF's financial statements is that the actual amount of the GRF's surplus changes to another amount chosen by the Government. This is worrisome because the Government uses the amount of the GRF's annual surplus or deficit as one of its key performance indicators.

In previous years, we recommended that the GRF's financial statements record transfers to the Fund as an asset, not as an expenditure and any transfers back to the GRF as a reduction of that asset, not as revenue.

In February 2002, The Standing Committee on Public Accounts (PAC) considered this matter and disagreed with our recommendation.

We continue to recommend that the General Revenue Fund's financial statements record transfers in accordance with Canadian generally accepted accounting principles for the public sector.

Loans Receivable reservation

The GRF's financial assets include loans receivable from Crown corporations of $3.6 billion. In some cases, these Crown corporations can only repay the loans due to the GRF if the Government gives them the money from the GRF to do so. GAAP for the public sector requires the Government to record such transactions as expenditures and not as loans receivable. At March 31, 2003, loans receivable from Crown corporations include $58 million that those corporations cannot repay unless the Government gives them the money to do so. An example is the loans to the Education Infrastructure Financing Corporation (EIFC). For further discussion of these loans, see the section of this chapter titled *Compliance with The Balanced Budget Act.*

The effect of not recording these transactions properly is as follows:

- the GRF's expenditures are understated by $58 million;
- the GRF's surplus is overstated by $58 million;

- loans receivable are overstated by $58 million; and
- accumulated deficit is understated by $58 million.

1. We recommend that the Government account for loans to Crown corporations in accordance with Canadian generally accepted accounting principles for the public sector.

Pension costs reservation

The GRF is responsible for the liabilities of several pension funds. However, the Government does not record these liabilities in the GRF's financial statements. Therefore, the Assembly and the public are unable to properly assess costs and liabilities because the financial statements do not include the GRF's total pension costs for the year or the unfunded pension liability. The financial statements only include the amounts the Government actually paid retired members or contributed to a pension fund that year. The effects of not properly recording pension costs are as follows:

- pension costs are understated by $24 million;
- the GRF's surplus is overstated by $24 million; and
- pension liabilities and accumulated deficit are understated by $4.0 billion.

In previous years, we recommended that the Government account for pension costs in the GRF's financial statements in accordance with Canadian generally accepted accounting principles for the public sector.

In February 2002, PAC considered this matter and disagreed with our recommendation.

We note that Manitoba is the only other provincial government in Canada that publishes financial statements that do not follow The Canadian Institute of Chartered Accountants accounting standards for pensions.

Compliance with *The Balanced Budget Act*

Finance did not prepare the annual update report in accordance with *The Balanced Budget Act* (Act).

The Act requires that after each general election, the Minister shall prepare a four-year financial plan. The Minister shall present the plan to the Legislative Assembly at the same time as the budget estimates. Over the four fiscal years covered by the plan, the forecast of total expenses covered by the plan must balance with or be less than the forecast of total revenues for the same four fiscal years. The Minister presented the plan to the Assembly as part of the March 2000 budget address.

Also, the Act requires the Minister to present an annual update report on the Government's progress with regard to the four-year plan. The Minister provides this annual update report as part of the Budget Summary. The Act states that if the accounting policies or practices of the Government change significantly, the Minister shall note the change in the next annual update report presented to the Assembly following the change. The Act states the Minister shall not use the change in determining whether the Government has met the objectives set out in the four-year financial plan. Instead, the Minister is to use the accounting policies and practices that existed at the start of the four-year plan.

During 2002-03, the Government established the Education Infrastructure Financing Corporation (EIFC). EIFC borrows from the GRF and in turn lends money to educational institutions to finance all or part of capital projects. Prior to the change, the GRF reported the cost of education capital projects as expenditures. In 2002-03, instead of reporting the cost of education capital projects as an expenditure, the GRF reported them as loans receivable due from EIFC. These receivables totalled $38 million. The Government intends to reduce the EIFC loan receivable annually by a fixed amount and to record that amount as an expenditure. This is a significant change to the accounting practices for the financing of education capital projects.

In March 2003, the Minister presented the third annual update report related to the four-year plan presented in 2000. The update report is set out in the following Exhibit.

GRF Financial Plan 2000-01 to 2003-04[3]				
(millions of dollars)	2000-01 (actual)	2000-02 (actual)	2002-03 (forecast)	2003-04 (budget)
Revenue	$ 6,753.6	$6,059.1	$ 6,404.5	$ 6,228.0
Operating Spending	5,256.8	5,721.2	5,784.4	5,970.6
Operating Surplus	1,496.8	337.9	620.1	257.4
Interest costs	664.1	616.8	618.0	650.0
Transfers (to) from the Fiscal Stabilization Fund	(775.0)	280.0	---	392.7
Budget Balance	57.7	1.1	2.1	0.1
Cumulative Balance	$ 57.7	$ 58.8	$ 60.9	$ 61.0

We expected the third annual update report to use the same accounting policies and practices that were in effect at the start of the four-year plan. However, the annual update did not use the same accounting policies and practices for capital projects financed by EIFC. Therefore, Finance did not prepare the annual update in accordance with the Act.

If the annual update had been prepared in accordance with the Act, the operating spending for 2002-03 would increase by $38 million to $5,822.4 million and the surplus would decrease by $38 million from $620.1 million to $582.1 million. Also, assuming no other changes were made, the budget balance would decrease by $38 million to a deficit of $35.9 million and the cumulative balance for 2002-03 would decrease to $22.9 million from $60.9 million.

We also note the 2003-04 Estimates show loans of $32.4 to EIFC and operating spending of $7.2 million for repayments of EIFC financed capital projects, resulting in a net spending of $25.2 million. If the annual update had been prepared in accordance with the Act, and assuming no other changes were made, the operating spending for 2003-04 would increase by $25.2 million to $5,995.8 million. Also, the resulting cumulative balance would show a deficit of $2.2 million instead of a surplus of $61.0 million.

[3] Exhibit from page 57 of the 2003-04 Budget Summary

2. **We recommend that Finance comply with *The Balanced Budget Act* by ensuring that the accounting policies and practices used to prepare the annual update report are consistent with those that were in place at the start of the four-year plan.**

In addition, the current balanced budget legislation focuses on balancing the financial results of only one fund of the Government – the GRF. Balancing the financial results for the GRF does not result in balanced financial results for the entire Government. If it is Government policy to have balanced budget legislation, the Government should consider legislation based on balancing the financial results for the entire Government.

Prior years' recommendations

Annual pension costs not included in Estimates

In previous reports, we reported that the Assembly and the public are unable to assess pension costs properly because the Estimates do not include the GRF's estimated total pension costs for the year. The Estimates only include the amounts that the Government expects to pay retired members or contribute to a pension fund that year.

The effects of not including the GRF's total pension costs in the Estimates for the year ended March 31, 2003 are as follows:

- budgeted operating expenditures of $5.7 billion are understated by $25 million;
- the GRF's budgeted surplus of $45,000 is overstated by $25 million; and
- the budgeted accumulated deficit of $7 billion is understated by $4.0 billion.

In previous years, we recommended that Finance include the GRF's total pension costs for the year in the Estimates.

In February 2002, PAC considered this matter and disagreed with our recommendation.

This matter is important because the Government uses the GRF's budgeted surplus or deficit as one of its key performance indicators. If the budgeted surplus or deficit does not include the total estimated pension costs, it is difficult for the Assembly and the public to assess the Government's performance. As well, the Assembly makes decisions based on the belief that the budget is balanced. It might make different decisions if the budget included the correct amount of pension costs for the year.

In March 2003, the Government announced it would present a summary financial plan for the entire Government as part of the 2004-05 budget package. Finance proposed a model for a summary financial plan that was conceptually similar to the model we proposed in our 2002 Fall Report – Volume 1. We are satisfied with Finance's proposed model. This model will include the Government's total pension costs in the summary financial plan.

Public Service Superannuation Board

The Public Service Superannuation Board (Board) is responsible for administration of *The Public Service Superannuation Act* and other related legislation. The Board's primary objective is to provide superannuation allowances to employees who retire, and to dependants of deceased superannuates and employees, in accordance with the law.

The Board manages the Public Service Superannuation Plan (Plan). The Plan consists of the Public Service Superannuation Fund, the Anti-Tuberculosis League Employees Superannuation Fund, and the Saskatchewan Transportation Company Employees Superannuation Fund. The Plan is a defined benefit final average pension plan.

In 2002-2003, the Plan received contributions of $5.5 million from employees and $88.5 million from the GRF. At March 31, 2003, the Plan held assets of $17.0 million and had liabilities of $1,594.3 million.

Rules and procedures needed to assess the pension obligation

The Board needs to ensure that management has adequate rules and procedures to assess the accuracy of its pension obligation.
Pension plans need periodic actuarial valuations of their pension obligations to prepare their financial statements. To calculate the pension obligations, actuaries use data that pension plans provide. Management is responsible to ensure that the data it provides to the actuary is complete and accurate. If the data is incomplete and inaccurate, it will result in an inaccurate calculation of the pension obligation. Management is also responsible to ensure that the data the actuary uses for the valuation is the data it provided.

The Board obtained an actuarial valuation as at December 31, 2002. The actuary extrapolated the results of the actuarial valuation to March 31, 2003 to value the pension obligation reported in the March 31, 2003 financial statements.

Management provided inaccurate and incomplete data to the actuary. The actuary calculated the valuation based on this data. Because management did not have rules and procedures to ensure the accuracy of its pension obligations, staff did not review the data provided to the actuary to ensure the data was complete and accurate. During our audit, we detected a number of errors in the data given to the actuary. The errors related to gender, length of service, salary, and indexing provisions. Management then supplied corrected data to the actuary. The revised data resulted in a $28.7 million reduction in the Plan's reported pension obligation as at March 31, 2003.

3. We recommend that the Public Service Superannuation Board establish rules and procedures to assess the accuracy of its pension obligation.

Retired members' pensions

The Board needs information about retired members of the Plan who are receiving a pension and have returned to work for the Government. The Board needs this information to ensure it pays pensions in accordance with the law.

Requirements for stopping the pensions of retired members who return to work for the Government are set out in Section 27 of *The Superannuation (Supplementary Provisions) Act* (Act). The Act allows retired members to work as temporary, casual, or provisional employees for up to six months per year without a reduction in their pension. However, the Act requires the Board to stop the pension of a retired member who works for the Government for more than six months in a year. The Act also requires the Board to stop the pension of a retired member that the Government re-hires as a permanent employee when that member starts work.

The Board does not have rules and procedures to know if retired members are working for the Government. The Board relies on retired members notifying the Board upon re-employment with the Government. As a result, the Board cannot ensure that all pensions paid comply with the law. Accordingly, we cannot determine if the Board complied with section 27 of the Act.

We reported this matter in both our 2001 Spring Report and 2002 Fall Report. In November 2001, PAC considered this matter and concurred with our recommendation.

We continue to recommend that the Public Service Superannuation Board establish rules and procedures to ensure that all retired members who are receiving a pension and return to work for the Government are paid in accordance with the Act. Alternatively, the Board should seek changes to the Act.

This page left blank intentionally.