

Main points	264
Introduction	265
Financial overview	265
Special purpose funds and Crown agencies	266
Key risks	267
Our audit conclusions and findings.....	267
Saskatchewan Agricultural Stabilization Fund	269
Reliability of the financial statements	270
Operations need monitoring	271
Saskatchewan Crop Insurance Corporation.....	272
Internal audit function needs strengthening.....	273
Pastures Revolving Fund	274
Budget process needs improvement	274
Financial reporting needs improvement	275
Manual needs improvement	277
Removal of livestock without payment	278
Horned Cattle Fund.....	278
Agreement needs monitoring	279

Main points

In this chapter, we report the results of the audit of the Department of Agriculture, Food and Rural Revitalization (Department) and the special purpose funds and agencies for which it is responsible.

The Department needs a process to oversee the operations of the Saskatchewan Agricultural Stabilization Fund. Inadequate and incomplete financial, operational, and compliance reports increase the risk of the Department making inappropriate decisions.

The Saskatchewan Crop Insurance Corporation's internal auditor needs to prepare an adequate work plan and have it approved by the Board. The plan should focus on the areas that present the greatest business risks to the Corporation.

The Department needs to improve its budgeting and financial reporting processes for the Pastures Revolving Fund. Also, it needs to update its policies and procedures manual to include guidance on preparing financial statements.

Finally, the Department needs to establish processes to monitor a research centre's use of public money.

Introduction

The mandate of the Department of Agriculture, Food and Rural Revitalization (Department) is “to foster a commercially viable, self-sufficient, and sustainable agriculture and food sector, and healthy and diverse rural communities. Working with individuals, businesses, communities, and governments, the Department assists farmers and ranchers, encourages higher value production and processing, and promotes sustainable economic and social development in rural Saskatchewan.”¹

Financial overview

The following table sets out the Government's total expenditures and revenues for the agricultural programs it administers through the Department and other agencies that the Government controls. The Government's summary financial statements for the year ended March 31, 2004 reflect this information.

	<u>2004</u>	<u>2003</u>
	(millions)	
Agricultural expenditures by program:		
Crop insurance	\$ 420	\$ 1,126
Farm stability	177	138
Other	<u>77</u>	<u>64</u>
	<u>\$ 674</u>	<u>\$ 1,328</u>
Agricultural revenues by source:		
Federal Government	\$ 176	\$ 565
Producers' crop insurance premiums	126	86
Interest on loans and investments	7	7
Sales, services, fees, permits, and other	<u>35</u>	<u>36</u>
	<u>\$ 344</u>	<u>\$ 694</u>

The Department's 2003-2004 Annual Report (available at <http://www.agr.gov.sk.ca>) contains information about the Department's revenues and expenditures. The Public Accounts compendium (see <http://www.gov.sk.ca/finance/paccts/>) reports the revenues and expenses

¹ Saskatchewan. Department of Finance. (2003). *2003-04: Saskatchewan provincial budget: building for the future: Estimates*. Regina: Author. page 25.

of the Department's special purpose funds and agencies listed below, except for agencies under the Agri-Food Council, which are reported in the Council's annual report.

Special purpose funds and Crown agencies

The Department is responsible for the following:

	<u>Year-end</u>
Agricultural Credit Corporation of Saskatchewan	March 31
Agri-Food Council	March 31
Agricultural Implements Board	March 31
Agri-Food Innovation Fund	March 31
Beef Development Board	March 31
Cattle Marketing Deductions Fund	March 31
Horned Cattle Fund	March 31
Individual Cattle Feeder Loan Guarantee	
Provincial Assurance Fund	March 31
Livestock Services Revolving Fund	March 31
Milk Control Board	December 31
Pastures Revolving Fund	March 31
Prairie Agricultural Machinery Institute	March 31
Saskatchewan Agricultural Stabilization Fund	March 31
Saskatchewan Crop Insurance Corporation	March 31
Crop Reinsurance Fund of Saskatchewan	March 31

Agencies under the Agri-Food Council

Saskatchewan Alfalfa Seed Producers' Development	
Commission	July 31
Saskatchewan Broiler Hatching Egg Producers'	
Marketing Board	December 31
Saskatchewan Canola Development Commission	July 31
Chicken Farmers of Saskatchewan	December 31
Saskatchewan Commercial Egg Producers'	
Marketing Board	December 31
Saskatchewan Flax Development Commission	July 31
Saskatchewan Mustard Seed Development Commission	July 31
Saskatchewan Pulse Crop Development Board	August 31
Saskatchewan Sheep Development Board	September 30
Saskatchewan Turkey Producers' Marketing Board	December 31
Sask Pork	July 31

Key risks

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

We identified the key risks the Department must manage well to be successful. The Department must ensure that:

- ◆ Saskatchewan is able to compete successfully in world agricultural markets;
- ◆ Saskatchewan's agricultural production and processing industries are sustainable and commercially viable;
- ◆ Saskatchewan's agricultural production and processing industries provide reasonable investment opportunities; and
- ◆ Saskatchewan's agricultural production and processing industries are adequately diversified from primary agricultural products to higher value products.

We identified the key risks through discussions with management and reviewing the Department's web site and annual report. Management confirmed that these are the key risks facing the Department. We have not audited the systems and practices the Department uses to manage its key risks.

Our audit conclusions and findings

This chapter contains our audit conclusions and findings for the Department for the year ended March 31, 2004 and for its special purpose funds and agencies with March 31, 2004 or July 31, 2004 year-ends where we participated in the audit.

We did not participate in the audits of agencies under the Agri-Food Council except for Sask Pork, Saskatchewan Canola Development

Commission, and Saskatchewan Mustard Seed Development Commission. Instead, as part of our audit of the Department, we examine the supervisory work carried out by the Council regarding those agencies' financial statements and their processes to safeguard public resources, and comply with legislative authorities.

Our Office worked with the following appointed auditors:

- ◆ KPMG LLP
 - Saskatchewan Agricultural Stabilization Fund
 - Saskatchewan Crop Insurance Corporation
 - Crop Re-insurance Fund of Saskatchewan
- ◆ Meyers Norris Penny LLP
 - Agricultural Credit Corporation of Saskatchewan
- ◆ Deloitte & Touche LLP
 - Sask Pork

To complete our work we used the framework recommended by the *Report of the Task Force on Roles, Responsibilities and Duties of Auditors* (see our web site at <http://www.auditor.sk.ca/rrd.html>). Our Office and the appointed auditors formed the following opinions.

In our opinion, for its special purpose funds and agencies with March 31, 2004 or July 31, 2004 year-ends where we participated in the audit:

- ◆ **the Department, its special purpose funds, and its agencies had adequate rules and procedures to safeguard public resources except for the Saskatchewan Agricultural Stabilization Fund, Saskatchewan Crop Insurance Corporation, Pastures Revolving Fund and Horned Cattle Fund;**
- ◆ **the Department, its special purpose funds, and its agencies complied with the authorities governing their activities relating to financial reporting, safeguarding public resources, revenue raising, spending, borrowing, and investing except for the Pastures Revolving Fund; and**

- ◆ **the financial statements of the Department's special purpose funds and agencies are reliable except for the Saskatchewan Agricultural Stabilization Fund. In KPMG's opinion, the financial statements of the Saskatchewan Agricultural Stabilization Fund are reliable.**

We did not rely on KPMG's opinion on Saskatchewan Agricultural Stabilization Fund's financial statements.

The Provincial Auditor Act requires us to do additional work when we are unable to rely on the report of an appointed auditor. Our additional work consisted of reviewing the agreements between Canada and Saskatchewan and discussion with the Department's management.

Saskatchewan Agricultural Stabilization Fund

The Department administers the Saskatchewan Agricultural Stabilization Fund (SASF).

SASF reports the transactions of the following seven programs:

- The New Crops Insurance Program
- The Big Game Damage Compensation Program
- The Waterfowl Damage Compensation Program
- The Agricultural Income Disaster Assistance Program (AIDA)
- The Canadian Farm Income Program (CFIP)
- The Canada-Saskatchewan Bovine Spongiform Encephalopathy Recovery Program (BSE)
- Canada-Saskatchewan Assistance Program

SASF's 2004 Annual Report includes its financial statements for the year ended March 31, 2004. Those financial statements report revenues of \$103.9 million and expenses of \$90.3 million. The financial statements also report net financial assets of \$23.6 million at March 31, 2004.

The Governments of Canada (Canada) and Saskatchewan agreed to share the costs of these programs. The Government of Saskatchewan (Saskatchewan) administers all the programs except AIDA and CFIP. Canada administers AIDA and CFIP. The laws governing these programs and the agreements between Canada and Saskatchewan require that all money paid into SASF can only be used for the purposes of these

programs. In addition, the Department must return any money received and not used to pay for program costs to Canada and Saskatchewan at the end of the programs. SASF operates on a break-even basis except for the interest income earned on advances, which it may keep. Accordingly, these advances received should be recorded as liabilities (i.e., as amounts owed back to Canada and Saskatchewan) until SASF incurs related program costs. When SASF incurs those program costs, it should deduct an equal amount from liabilities and record the amount as revenue to offset the program costs.

Reliability of the financial statements

The financial statements of SASF are not reliable.

SASF's 2004 financial statements overstate revenue and its annual surplus (i.e., annual income) for 2004 by \$2.8 million. Also, the financial statements understate SASF's liabilities (what it owes to others) by \$12.8 million. This information gives readers of the financial statements the wrong message. The message given is that revenues exceed expenses by \$13.6 million and that SASF has \$23.6 million on hand that it can keep because it is no longer required to pay for future program costs. In fact, SASF's revenues were lower than reported by \$2.8 million in 2004. In addition, it must either use \$12.8 million of the reported net assets to pay for future program costs or return the money to the General Revenue Fund (GRF).

The errors in SASF's financial statements result from the Department incorrectly recording transfers from the GRF. The Department correctly records all money received from Canada. The Department records revenue equal to Canada's share of program costs. The Department records money received from Canada in excess of its share of program costs as a liability owing to Canada until the Department incurs costs under the program. This accounting follows the accounting standards of The Canadian Institute of Chartered Accountants (CICA). However, the Department incorrectly records transfers received from the GRF. It records this money as revenue immediately, regardless of when the Department incurs the program costs.

The Department should record money received in advance as a liability and later as revenue when it incurs related program costs. Also, because

SASF operates on a break-even basis for the money received from Canada and Saskatchewan, its only net assets should be interest earned on advances.

We also reported this matter in our 2003 Report – Volume 3 and in previous reports.

We continue to recommend that the Department record money received from the GRF as a liability of SASF until it incurs the related program costs or until it returns the money to the GRF.

The Department thinks that because SASF and the GRF are part of the Provincial Government, any restrictions between them cannot be considered external. Therefore, the Department thinks it is appropriate to record the money received from Canada and the GRF differently.

We disagree. We think it is irrelevant that SASF and the GRF are part of the Provincial Government. The shared-cost agreements between Canada and Saskatchewan restrict the use of money contributed under those agreements for specific purposes. The GRF provided money under the agreements and until SASF spends the money for those purposes, it has a debt to the GRF.

On November 5, 2002, the Standing Committee on Public Accounts (PAC) deferred a decision on our recommendation pending the results of a CICA project that is examining accounting standards concerning government transfer payments. The CICA project is not finished.

Operations need monitoring

The Department needs to set up processes to oversee the SASF's operations.

The Department needs to define the financial, operational, and compliance reports necessary to monitor the operations of SASF. Financial reports should include SASF's financial statements and explain the differences between the planned and actual financial results. These reports should also project results expected for the remainder of the year. Operational reports should show its progress towards what the SASF

expects to achieve. Compliance reports should describe SASF's compliance with authorities (e.g., the law and policies).

The Department has not set out what financial, operational, and compliance reports it must receive regularly from those who manage SASF. Also, the Department has not set up a process to review those reports and give direction to staff.

Because the Department has not set out its reporting needs, SASF managers did not provide to the Department regular financial reports for SASF during the year. Nor did they provide regular operational and compliance reports on the activities of SASF.

Inadequate and incomplete financial, operational, and compliance reports increase the risk of inappropriate decisions.

- 1. We recommend that the Department of Agriculture, Food and Rural Revitalization set out the financial, operational, and compliance reports it needs to monitor the Saskatchewan Agricultural Stabilization Fund.**

Saskatchewan Crop Insurance Corporation

The Saskatchewan Crop Insurance Corporation (SCIC) pays producers for crop losses due to weather-related and other natural perils. The Government of Canada participates in this insurance program. The agreement dated April 1, 2003 with the Government of Canada set out how much the Federal Government would pay for this program. The program guarantees a minimum crop yield and quality of grain to agricultural producers, subject to specific insurance decisions made by each producer.

In 2004, SCIC held total assets of \$186.6 million, had revenues of \$276.5 million, and had expenses of \$275.7 million. SCIC's 2004 Annual Report (available at <http://www.saskcropinsurance.com>) includes its financial statements.

SCIC insured 30 million seeded acres and had 33,916 contracts for the 2003 crop year covering over 45 crops. SCIC incurred claim costs of \$242.7 million for crop losses.

SCIC also manages the Crop Reinsurance Fund of Saskatchewan (Fund). SCIC pays to the Fund a portion of its total premium revenue. When SCIC incurs losses, the Fund pays SCIC for part of the losses. In 2004, the Fund had revenue of \$41.7 million, expenditure of \$93.5 million, and had a deficit of \$134.2 million.

Internal audit function needs strengthening

SCIC needs to strengthen its internal audit function. To be effective, SCIC's internal auditor must provide assurance on the adequacy of the processes to safeguard public resources and to comply with the law. The auditor should focus work on the areas that present the greatest business risks to SCIC, e.g. premium rate setting processes.

Boards of agencies need independent assurance that management operates according to the board's direction. An independent internal auditor can provide such assurance. To be independent, the internal auditor should report directly to the board or to a committee of the board. Also, the internal auditor must provide audit plans including a risk assessment of all the agency's programs and activities for the board's approval. The Board should then receive regular reports from the internal auditor on audit findings.

SCIC's internal auditor focuses efforts on SCIC's adjusting claims processes. The internal auditor provides semi-annual reports to the Board. However, the Board does not receive and approve an audit plan for the internal auditor. The Board did receive some information about the internal auditor's work through SCIC's corporate plan and the internal auditor division's semi-annual reports.

To effectively oversee SCIC, the Board needs to receive an audit plan that includes a complete risk assessment of all SCIC's programs and activities. The Board can then determine if the proposed work plan adequately addresses all risks and provide adequate resources to the internal auditor.

2. We recommend that the Board of Directors of Saskatchewan Crop Insurance Corporation approve a work plan for its

internal auditor based on a risk assessment of the Corporation's activities.

Management told us it plans to improve its internal auditor's work plan.

Pastures Revolving Fund

The Pastures Revolving Fund (Fund) provides for the establishment, operation, management, and maintenance of pastures, programs, and services related to pasture and livestock management. It also provides programs related to developing, protecting, and promoting the environmental, social, and economic use of pastures.

For the year ended March 31, 2004, the Fund had revenues of \$6.5 million, expenses of \$6.2 million and held assets of \$2.9 million.

Budget process needs improvement

The Department did not prepare a detailed operational budget for the Fund that supports the estimates it sent to Treasury Board for approval. Treasury Board's policy is to approve the budgets of all revolving funds and any revisions to those budgets. According to paragraph 3210.26 of the Financial Administration Manual, revolving fund budgets are to include a detailed operational budget, i.e., a pro-forma income statement that outlines revenues, expenses, and resulting surplus/deficit and a cash flow budget.

Budgets are normally prepared and approved for the upcoming year in the fall. However, the Department did not prepare a detailed operational budget for the Fund's current year (2003-04) until March 2003. Therefore, in October 2002, the Department only gave Treasury Board estimates of the Fund's total revenue and total expense. The Department did not document how it determined these two estimates. Treasury Board approved the Department's budget submission with those estimates.

When the Department prepared the detailed 2003-04 budget for the Fund, it differed significantly from the revenue and expense totals approved by Treasury Board. For example, budgeted revenue was \$645,000 less than the approved amount and budgeted expenses were \$310,000 higher than the approved amount. The Department did not send

these revisions to Treasury Board for approval. The Department then changed some of the Fund's detailed budget figures to make the totals agree with those approved by Treasury Board. The Department used this incorrect budget to manage the Fund and prepare financial reports. When an agency uses incorrect budgets in internal and external financial reports to manage operations or explain variances, there is an increased risk of making inappropriate decisions.

Adequate guidance for preparation of the Fund's budget is set out in the Fund's Policies and Procedures Manual. Following this guidance would satisfy the requirements set out in the Financial Administration Manual. However, staff did not comply with the established guidance to prepare the budget.

The Department should prepare a detailed budget for the Fund in the fall to support the information before sending it to Treasury Board for approval. Alternately, the Department should submit the detailed budget it prepares in March to Treasury Board for approval. The Department should use forecasts to manage any changes that arise later. This will ensure that the Fund's approved budget appropriately reflects its planned operations. It will also allow the Department and Treasury Board to review the Fund's actual performance against the approved plan.

- 3. We recommend that the Department of Agriculture, Food and Rural Revitalization prepare a detailed budget for the Pastures Revolving Fund to support the estimates information before sending it to Treasury Board for approval.**

Financial reporting needs improvement

In 2003-04, the Department did not prepare financial statements that accurately reflect the Fund's financial position and operating results.

The Financial Administration Manual states that the Fund's financial statements must be prepared in accordance with Canadian generally accepted accounting principles (GAAP). It also requires revolving funds to prepare and submit quarterly financial statements to Treasury Board.

Staff did not prepare the Fund's year-end financial statements in accordance with GAAP. An adequate review of the supporting information

used to prepare the financial statements would have identified the information that was incorrect or insufficient. The financial statements presented for audit contained three significant errors as follows:

- ◆ the unearned portion of billings for petroleum leases was not recorded as a liability;
- ◆ some capital assets were not properly classified or amortized; and
- ◆ accounts receivable was not properly valued.

As a result, the financial statements presented for audit contained the following misstatements:

- ◆ accounts receivable was understated by \$57,500;
- ◆ capital assets was understated by \$28,700;
- ◆ unearned revenue was understated by \$331,100;
- ◆ accounts payable was understated by \$46,800;
- ◆ accumulated operating deficit was understated by \$280,600;
- ◆ amortization expense was understated by \$10,500;
- ◆ repairs and improvements expense was overstated by \$39,200; and
- ◆ bad debt expense was overstated by \$68,700.

We worked with the Department to quantify these errors and it corrected the financial statements. However, the correction of these errors and the audit of the revised financial statements took an additional two months. As a result, the Department was unable to comply with the June 29, 2004 deadline for submission of audited financial statements to its Minister, as set out in *The Tabling of Documents Act, 1991*. The final draft financial statements were completed and submitted to Treasury Board for approval on August 27, 2004.

Also, the Department did not prepare quarterly financial statements using GAAP for submission to Treasury Board. Instead, the Department managed the Fund using income and expense reports prepared on the cash basis. Incorrect or inadequate financial statements increase the risk of making incorrect management decisions. Also, the Department should improve its rules and procedures to ensure that management adequately reviews the supporting documentation used to prepare the financial statements.

- 4. We recommend that the Department of Agriculture, Food and Rural Revitalization prepare the Pastures Revolving Fund’s financial statements in accordance with Canadian generally accepted accounting principles.**

Manual needs improvement

The Department needs to update the Fund’s Policies and Procedures Manual to include guidance for financial reporting.

Written guidance forms part of an agency’s system of internal control. Usually, an accounting policies and procedures manual provides such guidance. This manual can be a guide to staff as they carry out their duties. Recorded policies and procedures help in the orderly and efficient conduct of business and help ensure financial reports are accurate.

An accounting policies and procedures manual should include:

- ◆ a description of the information needs of senior management and central agencies;
- ◆ job descriptions for all staff positions including delegated authority levels;
- ◆ a description of the significant accounting policies together with procedures necessary to ensure financial reports are properly prepared in accordance with GAAP; and
- ◆ detailed administrative control procedures for all accounting systems.

In prior years, we reported that the Department needed to prepare a complete accounting policies and procedures manual for the Fund. It did so, but recently removed key material related to the preparation of financial reports. The misstatements in the Fund’s financial statements noted above are due in part to this lack of guidance to staff on the preparation of financial reports.

- 5. We recommend that the Department of Agriculture, Food and Rural Revitalization include guidance for financial reporting in the Pastures Revolving Fund’s Policies and Procedures Manual.**

Removal of livestock without payment

The Department did not follow the law when it permitted patrons to remove their livestock from government-operated pastures without full payment of their accounts.

Subsection 22(7) of *The Pastures Regulations* states that patrons must pay all outstanding fees before removing livestock from a pasture. In 2003-04, Department officials directed pasture managers to waive this requirement. They told us this was due to financial hardship faced by livestock producers. Consequently, the Department permitted patrons who owed a total of \$935,000 to remove their livestock from pastures without full payment of all outstanding fees. Instead, it accepted cheques post-dated for up to six months, considering that to be payment. The Department has since collected substantially all of the amounts owing.

The method to amend a regulation (permanently or temporarily) is to seek Cabinet approval (i.e., an Order in Council). The Department should have obtained an Order before changing the fee collection policy set out in the law.

- 6. We recommend that the Department of Agriculture, Food and Rural Revitalization comply with *The Pastures Regulations* for the payment of outstanding pasture fees.**

Horned Cattle Fund

The Horned Cattle Purchases Act established the Horned Cattle Fund (Fund). The purpose of the Fund is to promote research and development in the livestock industry and to pay the Fund's administration expenses.

The Minister of Agriculture and Food (Minister) appointed the Horned Cattle Purchases Act Advisory Committee to administer the Fund. The Department of Agriculture, Food and Rural Revitalization (Department) manages the operations of the Fund.

For the year ended March 31, 2004, the Fund had revenue of \$290,705, expenses of \$336,028 and held net assets of \$177,287 at year-end.

Agreement needs monitoring

The Department needs to know that the money it gives to research centres is safeguarded and used for authorized purposes.

The Minister made a five-year agreement with a research centre on November 1, 2001. Under the agreement, the Fund loaned cattle to the centre for research purposes. The agreement allows the centre to sell these cattle to generate research funds. The money received from the sale of these cattle belongs to the Department. The Department receives this money and pays an equal amount back to the centre for research purposes. For the year ended March 31, 2004, the centre reported that it collected revenue of \$195,064 and incurred expenses of \$195,064 for the Fund.

The Department does not have processes to know whether the centre properly safeguards public resources and complies with the terms of the agreement. In 2002, the Department instructed its staff to begin regularly monitoring the centre without specifying the monitoring procedures that they must do. Department staff monitored the centre for the year ended March 31, 2003 by reviewing the centre's accounting records and analyzing the reasonability of the centre's spending. However, for the year ended March 31, 2004, we did not see evidence of such monitoring. Accordingly, the Department does not know if the centre properly safeguarded public resources and complied with the terms of the agreement.

- 7. We recommend that the Department of Agriculture, Food and Rural Revitalization establish rules and procedures to know whether the money it gives to research centres is safeguarded and used for authorized purposes.**

This page left blank intentionally.