Finance

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Main points

The Ministry of Finance manages almost $5 billion of investments for the General Revenue Fund, the Growth and Financial Security Fund, and several other agencies. Finance sets aside a significant amount of money in investments to repay the Government's debt. The success of its investing activities can have a significant impact on the Government's financial position.

Finance has not sufficiently set out its investing expectations to enable it to evaluate its performance in managing investments. While it has investment guidelines, it does not report on its compliance with those guidelines. Also, the public does not receive reports on the performance of Finance's investing activities.

Where Finance carries out investing activities for others, it has not agreed with them, in writing, on their roles and responsibilities. Also, because of low turnover of staff who carry out investing and borrowing activities, Finance has not sufficiently documented its procedures. To protect itself from a possible disruption of investing and debt management services in the event of staff turnover, it should document these procedures.

Finance is responsible for 25 special purpose funds and agencies. This report covers 17 of those funds and agencies with a December year-end. These agencies have reliable financial statements, have complied with the law, and have adequate rules and procedures with the following exceptions.

For six employee benefit plans, the Public Employees Benefit Agency did not review or approve monthly bank reconciliations and journal entries on a timely basis. The Agency needs to set policies for the preparation and approval of bank reconciliations and journal entries.

Introduction

The Ministry of Finance (Finance) helps the Government manage and account for public money. As part of these duties, Finance administers and is responsible for several special purpose funds and agencies.

Special purpose funds and Crown agencies

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

Year ended December 31
Extended Health Care Plan
Extended Health Care Plan for Certain Other Employees
Extended Health Care Plan for Certain Other Retired Employees
Extended Health Care Plan for Retired Employees
Municipal Employees' Pension Commission
Municipal Financing Corporation of Saskatchewan
Public Employees Deferred Salary Leave Fund
Public Employees Dental Fund
Public Employees Disability Income Fund
Public Employees Group Life Insurance Fund
Saskatchewan Government Insurance Service Recognition Plan
Saskatchewan Pension Plan
Saskatchewan Power Corporation Designated Employee Benefit Plan
Saskatchewan Power Corporation Pre-1996 Severance Plan
Saskatchewan Water Corporation Retirement Allowance Plan
SaskEnergy Retiring Allowance Plan
SaskPower Supplementary Superannuation Plan

Year ended March 31
Growth and Financial Stability Fund
General Revenue Fund
Judges of the Provincial Court Superannuation Plan
Public Employees Benefits Agency Revolving Fund
Public Employees Pension Plan
Public Service Superannuation Plan
Saskatchewan Pension Annuity Fund
Saskatchewan Watershed Authority Retirement Allowance Plan

This chapter contains our audit conclusions and findings for the agencies with years ended December 31, 2008 and findings related to our audit work on the Ministry's treasury management activities. Our Office did this work at the request of the Deputy Minister of Finance and because of Finance's increased amount of investing activity. Our 2008 Report - Volume 3 includes the results of our audits of the agencies with years ending March 31, 2008.

Audit conclusions and findings

To form our opinions, our Office worked with Meyers Norris Penny LLP, the appointed auditor for Municipal Employees' Pension Commission and Deloitte & Touche LLP, the appointed auditor for Saskatchewan Pension Plan (Plan). We used the framework recommended by the *Report of the Task Force on Roles, Responsibilities and Duties of Auditors.*[1]

We did not rely on Deloitte & Touche's opinion on the adequacy of the Plan's rules and procedures to safeguard public resources because it did not report the need to complete the documentation of the Plan's information technology processes. *The Provincial Auditor Act* requires us to do additional work when we are unable to rely on the reports of an appointed auditor. Our additional work consisted of reviewing the Plan's information technology security processes and discussions with management.

In our opinion, for the year ended December 31, 2008:

- **Finance and its agencies with a December year-end had adequate rules and procedures to safeguard public resources except for matters reported in this chapter**
- **Finance and its agencies with a December year-end complied with authorities governing their activities relating to financial reporting, safeguarding public resources, revenue raising, spending, borrowing, and investing**
- **the financial statements of agencies with a December year-end are reliable**

[1] To view a copy of this report, see our website at www.auditor.sk.ca/rrd.html.

Employee benefit plans

Background

The Public Employees Benefit Agency (PEBA), a division of Finance, administers various employee benefit plans as authorized by Cabinet under *The Financial Administration Act, 1993.* The audit findings in this section relate to the following plans:

- Extended Health Care Plan
- Extended Health Care Plan for Certain Other Employees
- Extended Health Care Plan for Certain Other Retired Employees
- Extended Health Care Plan for Retired Employees
- Public Employees Disability Income Fund
- Public Employees Group Life Insurance Fund

Need adequate policies for bank reconciliations and journal entries

PEBA did not independently review or approve monthly bank reconciliations and journal entries on a timely basis.

Regular reconciliation and review of recorded bank balances to bank records provides a check that all charges to the bank accounts are proper, all money due is received, and deposits are made to the correct bank account. Furthermore, under Section 3610 of Financial Administration Manual,[2] agency officials are responsible to independently review monthly bank reconciliations and provide approval in writing.

The preparation and review of journal entries helps ensure that adjustments to recorded account balances are correct and authorized.

PEBA has written policies for the preparation and review of bank reconciliations and journal entries. However, these policies do not specify when this work must be done.

[2] The Financial Administration Manual communicates to ministries and public agencies, Treasury Board's policies and the Provincial Comptroller's directives for the control, management and accounting of government financial resources. It is available at http://www.finance.gov.sk.ca/fam.

For the six employee benefit plans listed above, we identified instances where PEBA did not promptly review and approve bank reconciliations and journal entries or leave evidence that independent reviews and approvals were done.

Without adequate policies governing the preparation and approval of bank reconciliations and journal entries, there is increased risk that PEBA may not promptly detect errors or fraud in the employee benefit plans' bank balances and accounting records.

1. We recommend the Public Employees Benefits Agency implement adequate policies governing the preparation and approval of bank reconciliations and journal entries.

Management informed us that timely reviews and approvals did not occur during the year because of higher than normal staff turnover and additional time required to hire and train new staff. Also, management told us that all bank reconciliations and journal entries have now been reviewed and approved.

Municipal Employees' Pension Commission

Background

The Municipal Employees' Pension Commission (Commission) administers the Municipal Employees' Pension Plan which provides retirement benefits to members. The Commission contracted PEBA to provide day-to-day administration of the Plan.

Disaster recovery plan needed

In our 2007 Report – Volume 1, we recommended the Commission have a written, tested, and approved disaster recovery plan. In June 2007, the Standing Committee on Public Accounts (PAC) considered this matter and agreed with our recommendation.

The Commission depends on its computer systems to provide critical services. These services include receiving and recording contributions from employers, handling transfers of funds, and providing benefit payments to members. The Commission must be able to provide these services even if a disaster disrupts its operations and services. Without an adequate disaster recovery plan, the Commission may not be able to provide these critical services.

The Commission continues to develop a disaster recovery plan. In 2008, the Commission further documented its procedures for backup and recovery and tested the effectiveness of some of these procedures. Management told us it expects to complete the disaster recovery plan in 2009.

We continue to recommend the Municipal Employees' Pension Commission have a written, tested, and approved disaster recovery plan.

Saskatchewan Pension Plan

Background

The Saskatchewan Pension Plan (Plan) is a voluntary plan available to persons between 18 and 71 years of age. Contributions to the Plan are used to provide members with a pension at retirement.

The Plan's 2008 annual report includes its audited financial statements for the year ended December 31, 2008. In 2008, the Plan had contributions of $7.2 million, payments to pensioners of $7.5 million, and net assets of $160 million.

Security policies and procedures for information technology need improvement

In our 2008 Report – Volume 1, we reported that the Plan needed to approve information technology (IT) security policies and procedures that are based on a documented threat and risk assessment. In August 2008, PAC agreed with our recommendation.

IT security policies and procedures help ensure the confidentiality, integrity, and availability of information systems and data. The Plan's information system contains sensitive data including personal information on plan members.

The Plan has made significant progress on addressing this recommendation. It has drafted a new IT security policy for Board approval that is risk-based and sets out the key roles and responsibilities for security and its management. The Plan is working on documenting the security procedures needed to support this policy. Management told us it expects to complete this work by the end of 2009.

We continue to recommend the Saskatchewan Pension Plan approve information technology security policies and procedures that are based on a documented threat and risk assessment.

Treasury management

Background

Finance's Treasury and Debt Management Division manages the debt and cash position of the General Revenue Fund (GRF) and the Growth and Financial Security Fund. It also provides investment management services for the GRF and various other agencies (see Exhibit 1).

At March 31, 2008, Finance managed $4.7 billion in investments; these investments earned about $127 million in 2007-08. The table below sets out the investment totals and related income.

	Balance March 2008 (millions)	Income 2007-08 (millions)
GRF – temporary investments	$ 666	$ 11
GRF – sinking funds[3]	1,359	62
Fiscal Stabilization Fund[4]	1,529	39
Saskatchewan Infrastructure Fund[4]	105	5
Investments managed for other agencies (see Exhibit 1)	1,115	10
Total	$ 4,774	$ 127

[3] Sinking funds are money set aside for the repayment of debt. The GRF holds this money primarily in long-term investments.
[4] On May 14, 2008, when *The Growth and Financial Security Act* came into force, investments previously held in the Fiscal Stabilization Fund and Saskatchewan Infrastructure Fund were transferred to the Growth and Financial Security Fund. By law, the General Revenue Fund receives any investment income earned on these investments.

Setting investment expectations and measuring performance

Finance has not set out its expectations in sufficient detail to make possible an evaluation of its performance in managing investments.

The Financial Administration Act, 1993 makes the Investment Board[5] (a committee of Cabinet) responsible for all matters relating to investments and provides Finance with broad guidance on the nature of permissible investments. Finance has approved investment guidelines (i.e., Sinking Fund Investment Policy and Money Market Investment Guidelines) that set out its investment philosophy, investment objectives, investment limits (e.g., asset mix, prohibited investments) and, on a broad basis, its risk tolerance. It uses the Sinking Fund Investment Policy to guide its investment activities for the Growth and Financial Security Fund.

Finance's investment guidelines are consistent with generally established investing practices except for the following areas. Finance's guidelines do not:

- ♦ set out either investment return expectations or benchmarking guidelines that could be used to measure the achievement of its stated investment objectives
- ♦ require periodic evaluation of investment performance
- ♦ require staff involved in investing activities to adhere to standards of ethical conduct (such as disclosure of conflict of interests or restriction on personal investing activities)
- ♦ for sinking fund investments, require monitoring and reporting on compliance with the guidelines
- ♦ set limitations on securities lending activities[6]
- ♦ require periodic reporting to senior management or Treasury Board on compliance with investment limits, assessment of investment risks (e.g., risks arising from changes in credit rating or liquidity), or overall investment performance.

Finance needs to set out measurable expectations so its investment activities can be evaluated. We noted that Finance provides the Deputy Minister with general information on capital market activities each week

[5] The Investment Board is not active; rather staff advised us that Treasury Board (which has the same members as the Investment Board) carries out the Investment Board's responsibilities.
[6] Securities lending is where one party lends its securities (investments) to another.

and the Deputy Minister and Treasury Board with quarterly comparisons of actual to budgeted investment income. We did not find evidence that the Deputy Minister and Treasury Board received information on whether the investing activities met expectations or information on the Government's exposure to investment-related risks (e.g., credit risk). Also, we did not find evidence that senior management expects its internal audit group to periodically review the Ministry's treasury management procedures.

2. We recommend the Ministry of Finance set out its investment expectations in sufficient detail to make possible the measurement and evaluation of its investment performance.

3. We recommend the Ministry of Finance report to its senior management (e.g., Deputy Minister) and Treasury Board, at least quarterly, on its compliance with its investment guidelines and expectations.

4. We recommend the Ministry of Finance periodically carry out an internal audit to assess and report to senior management on compliance with its investment guidelines and expectations.

A key part of treasury management is deciding when to borrow, invest, or repay debt. Finance continuously monitors the market and maintains a five-year forecast of cash flows (e.g., capital spending, sinking fund instalments, and debt repayments) and daily cash flow forecasts to help guide these trade-off decisions. It develops a high-level annual financing strategy reviewed by senior management and receives direction from Treasury Board and Cabinet. Finance officials also advised us that they try to anticipate the impact of the market on various borrowing options and provide reports to Treasury Board upon its request.

How the Government manages its investments is a critical aspect of managing its debt. Strategies that link debt management with investing activities increase the importance of minimizing the risk of loss on investments and earning a return on its investments that covers the cost of servicing the debt.

The Government typically sets aside money in sinking funds as a way to help it repay the debt. The Government has historically bought and held a small amount of its own debt as investments in sinking funds.

At March 31, 2008, just over 60% of investments that Finance managed were held in sinking funds and in the Growth and Financial Security Fund. The Government's investments held in sinking funds at March 31, 2008 equalled about 12% of the GRF gross debt[7] and are forecast to be 30% of gross debt at March 31, 2009. At March 31, 2008, about 32% of its investments in sinking funds were its own debt (i.e., Government of Saskatchewan debentures).

	March 31, 2008 Actual ($ in millions)	March 31, 2009[8] Forecast ($ in millions)
Gross debt	11,578	11,285
Investments held in sinking funds	1,359	3,351
Saskatchewan debt held as investments in sinking funds	442	526

In 2007-08, the Government borrowed $626 million and repaid $1,071 million.[9] In 2008-09, it expects to borrow $378 million and repay about $738 million of debt.[10]

At March 31, 2008, almost 91% ($10,355 million) of the gross debt was non-callable (i.e., cannot be redeemed before its maturity by the issuer) with an average coupon rate of 6.47%.[11] The remaining gross debt is callable and comprised almost entirely of Canada Pension Plan debentures ($799 million) maturing in up to 27 years with an effective interest rate of 8%.

[7] In this chapter, gross debt refers to borrowing with debt instruments such as promissory notes and Government of Saskatchewan debentures. It does not include other amounts the Government owes, e.g., amounts owed for pensions.
[8] Saskatchewan Provincial Budget 2009-10 Budget Summary, Government of Saskatchewan, p.61.
[9] Government of Saskatchewan – 2007-08 Public Accounts, p. 38.
[10] Saskatchewan Provincial Budget 2009-10 Estimates, Government of Saskatchewan, p.13.
[11] Compiled from Government of Saskatchewan – 2007-08 Public Accounts, Supplementary Information, pp. 110-114.

In the fall of 2008, the Government announced its plans to reduce debt. It stated "debt reduction will be implemented by setting aside amounts in sinking funds."[12] This strategy to reduce debt by primarily setting aside amounts in sinking funds as opposed to reducing debt by other means (such as calling existing debt, or buying and holding a greater amount of its debt as investments) increases the importance of monitoring the success of its sinking fund investing activities.

In 2007-08, Finance achieved the following average rates of return on its investments: sinking funds – 4.76%; Fiscal Stabilization Fund – 4.34%; Saskatchewan Infrastructure Fund – 4.46%. In the same time period, the average cost of servicing the GRF gross debt was 6.7%[13] with the interest rate on long-term debt issued during 2007-08 ranging from 4.20% to 4.65%.

Finance officials told us that they expected to earn a reasonable return on its sinking fund investing activities. We did not find evidence that Finance set out a measurable return approved by senior management. We did not find evidence that Finance regularly compared actual return on investments to an expected rate of return or to the cost of servicing its debt.

5. We recommend the Ministry of Finance monitor and report publicly on the performance of the investments in its sinking funds.

Agreements for investment services needed

Finance has not completely documented its responsibilities when it provides investment services to other agencies.

Finance provides investment services for the agencies listed in Exhibit 1. At March 31, 2008, these agencies held investments totalling just over $1.1 billion. Finance notes that it has provided services to most of these agencies for many years.

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[12] Available at: http://www.gov.sk.ca/adx/aspx/adxGetMedia.aspx?mediaId=602&PN=Shared (14 Apr 2009).
[13] Average cost of servicing gross debt using the effective interest rate. Per Public Accounts 2007-08 Volume 1 (p. 59), the GRF's total interest costs were $787 million.

Exhibit 1 - Agencies for which Finance manages investments

Government agencies:
Agricultural Credit Corporation of Saskatchewan
Saskatchewan Centre of the Arts
Crown Investments Corporation of Saskatchewan
First Nations and Métis Fund Inc.
Health Quality Council
Investment Saskatchewan Inc.
Municipal Financing Corporation
Public Employees Dental Fund
Saskatchewan Crop Insurance Corporation
Saskatchewan Housing Corporation
Saskatchewan Institute of Applied Science and Technology
Saskatchewan Telecommunications
Saskatchewan Watershed Authority
Various Extended Health Care Plans
Non-government agencies:
Meewasin Valley Authority
Regina Pioneer Village

For most of these agencies, their own legislation gives them authority to invest but limits the types of investments to those authorized for the investment of moneys in the GRF under *The Financial Administration Act, 1993*. For a few, such as the Health Quality Council, Treasury Board has the right to direct their investments. For a few others, such as Crown Investments Corporation of Saskatchewan, Cabinet has the right to appoint the Minister of Finance or another person to handle the agency's investing.

When agencies decide to use Finance to make their short-term investments, Finance meets with them to discuss their investment needs and provides them with a written summary that briefly outlines investment services it expects to provide.

The summary sets out some but not all of the responsibilities associated with the investment services. It sets out:

- who pays costs associated with making the investment (transaction costs)
- the agency's responsibility to have sufficient authority to make investments and to pay for all investment purchases
- the guidelines Finance uses when making investments (i.e., Money Market Investment Guidelines)
- the timing of Finance's daily investing procedures
- the reporting of investment transactions by Finance to the agency

The summary places the onus on the agency to inform Finance of any investing restrictions. However, the summary is silent with respect to Finance reporting to the agency on its compliance with the investing guidelines.

Also, as mentioned in the summary, the objective of Finance's Money Market Investment Guidelines is "to earn an optimal rate of return for clients over a market cycle, within acceptable risk tolerances." Finance has not defined or reached an agreement or common understanding with each of these agencies on the "optimal rate of return" or "acceptable risk tolerance." Also, Finance's reports to agencies do not set out the actual rate of return achieved or investment risk assumed through the investment portfolio.

Because most agencies have used Finance's services for many years, the importance of setting out the key roles and responsibilities of each party in writing is increased. Documentation helps ensure that, over time, each party continues to have a clear understanding of their respective roles and responsibilities. Also, it provides a way to make certain each party has a common understanding of the nature, timing, and scope of services to be provided and provides an efficient means to evaluate and adjust those services to address changes in needs.

6. We recommend the Ministry of Finance agree on respective roles and responsibilities, in writing, with agencies that receive its investment services.

Documenting procedures

Finance does not have comprehensive documented procedures of its investment and borrowing management processes (treasury management functions).

Because turnover of staff that carry out investing and borrowing activities within the Ministry is low, many of its processes are only partially documented. Working practices tend to be passed on from employee to employee as part of on-the-job learning, rather than being written down. As a result, a large amount of institutional knowledge of investing and borrowing processes is not adequately documented. We note that Finance maintains detailed guidance on its cash flow forecasting procedures.

Also, staff do not always document the completion of key procedures. For example, senior management do not leave evidence of their review of sinking fund activity reports. Lack of documented detailed procedures could hamper the ability of Finance to continue with little interruption in its treasury management functions in the event of staff turnover.

7. We recommend the Ministry of Finance document its key treasury management procedures in sufficient detail so it can continue to operate effectively after staff turnover.

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