

**2004**  
**Report of the**  
**AUDITOR GENERAL**  
**to the**  
**Legislative Assembly**



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**Prince Edward Island**

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# INTRODUCTION

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## REPORT OVERVIEW

The Audit Act requires the Auditor General to report annually to the Legislative Assembly. This Annual Report 2004 provides observations, recommendations and information pertaining to the audits and examinations of government operations conducted by the Office during the year. The purpose of this report is to assist the Legislative Assembly in carrying out its responsibility to hold the government accountable for the management of public resources.

This Annual Report deals mainly with matters pertaining to the 2002-2003 fiscal year, however, many of the issues identified remain current and are still being addressed by government.

It is not possible to audit all government programs and entities each year, however, the office strives to provide reasonable audit coverage on a cyclical basis. A large portion of the audit work is determined by statutory requirements which name the Auditor General as auditor. These requirements include the annual audit of the Public Accounts of the Province. The remainder of our resources are devoted to special audits and examinations.

This report includes information and discussion on the **Province's Finances**. The section on **Special Audits and Examinations** summarizes the results of various examinations conducted during the year including; Crown Agencies-Control and Accountability, Information Technology Security Review, Construction of the Atlantic Technology Centre, Government Garages, Water Management Division, and Federal Claims. The **Financial Statement Audits** section provides information on significant issues arising from the financial statement audits conducted by the Office.

Each year we contact departments and agencies to obtain follow-up information on the status of any outstanding recommendations from previous years. This information is included in a separate section of the report, **Update on Previous Recommendations**.

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## Introduction

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The **Standing Committee on Public Accounts** reviews the Auditor General's Annual Report and plays an important role in holding government accountable for the management of public resources. Information on the role of this Committee, and its proceedings during the past year, is provided in a separate section of the report.

The section on the **Office of the Auditor General** provides information on the mission and mandate of the Office, as well as the responsibilities of the Auditor General. Background information is provided on the objectives and accomplishments of the Office as well as the resources used to achieve them.

## ACKNOWLEDGEMENTS

Cooperation of Ministers, Deputy Ministers, heads of Crown agencies and their staff is important. In carrying out our work we received the necessary information, reports and explanations. I wish to acknowledge this cooperation in the completion of the audits covered in my Annual Report.

I would like to express appreciation to my staff for their effort and commitment over the past year. The foundation of this Report and the recommendations therein are based on their professionalism, input and dedication.

# INTRODUCTION

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## VUE D'ENSEMBLE DU RAPPORT

La *Audit Act* (loi sur la vérification) impose au vérificateur général de faire rapport annuellement à l'Assemblée législative. Le présent rapport annuel 2004 contient des observations, recommandations et renseignements se rapportant aux vérifications et aux examens des activités du gouvernement, lesquels ont été menés par notre Bureau au cours de l'année. Le but de ce rapport est d'aider l'Assemblée législative à s'acquitter de sa responsabilité de tenir le gouvernement responsable de sa gestion des ressources publiques.

Ce rapport annuel traite principalement de sujets se rapportant à l'exercice financier 2002-2003. Toutefois, plusieurs des questions identifiées demeurent actuelles et le gouvernement ne cesse de les étudier.

Il est impossible de vérifier tous les programmes et entités du gouvernement chaque année; toutefois, le Bureau s'efforce de fournir un volume de vérification raisonnable sur une base cyclique. Une bonne partie du travail de vérification est précisée par les obligations légales imposées au vérificateur général à titre de vérificateur. Ces obligations comprennent la vérification annuelle des comptes publics de la province. Ce qui reste de nos ressources s'occupe à des vérifications et examens spéciaux.

Ce rapport comprend des renseignements et des discussions sur les **Finances de la province**. La section portant sur les **Vérifications et examens spéciaux** résume les résultats des divers examens menés durant l'année, notamment : le contrôle et la responsabilité des organismes de la Couronne, l'examen de la sécurité de la technologie de l'information, la construction du Centre de technologie de l'Atlantique, les garages du gouvernement, la Division de la gestion des eaux et les réclamations fédérales. La section traitant des **Vérifications des états financiers** fournit des renseignements sur les problèmes importants soulevés par les vérifications des états financiers menées par le Bureau.

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## Introduction

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Chaque année, nous communiquons avec les organismes et ministères pour obtenir un complément d'information sur l'état des recommandations en souffrance des années antérieures. Ces renseignements font partie d'une section distincte du rapport intitulée **Mise à jour des recommandations précédentes**.

Le **Comité permanent des comptes publics** examine le rapport annuel du vérificateur général et joue un rôle important pour tenir le gouvernement responsable de la gestion des ressources publiques. Les renseignements sur le rôle de ce Comité, et ses délibérations au cours de la dernière année, sont fournis dans une section distincte du rapport.

La section traitant du **Bureau du vérificateur général** fournit des renseignements sur la mission et le mandat du Bureau, ainsi que sur les responsabilités du vérificateur général. On y trouve des renseignements de base sur les objectifs et les réalisations du Bureau ainsi que sur les ressources utilisées à ces fins.

## REMERCIEMENTS

La collaboration des ministres, des sous-ministres, des chefs des organismes de la Couronne et de leur personnel est importante. Dans l'exécution de notre travail, nous avons reçu les renseignements, les rapports et les explications nécessaires. J'aimerais exprimer ma gratitude pour cette collaboration dans l'exécution des vérifications mentionnées dans mon rapport annuel.

J'aimerais également témoigner mon appréciation à mon personnel pour ses efforts et son engagement au cours de la dernière année. Les assises du présent rapport et les recommandations qu'il contient sont fondées sur son professionnalisme, sa contribution et son dévouement.

# 1. THE PROVINCE'S FINANCES

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## OVERALL COMMENTS

**1.1** Each year we comment on the Province's finances. The financial position of the Province for the most recent fiscal year is discussed and compared over a five year period. To assess the financial condition of the Province it is necessary to focus on the financial results in the Consolidated (Summary) Financial Statements. These statements report the full nature and extent of the financial affairs and resources for which the Government is responsible. The financial position of the Province is important because it provides an assessment at a point in time of the Government's management of its financial affairs and resources as a whole. Creditors also use it to establish a credit rating which determines the cost of borrowing for the Province; the lower our credit rating the higher the interest rates to service our debt.

**1.2** In the last year the Provincial gross domestic product increased by 7.9 percent while the net debt increased by 7.7 percent. Despite economic growth the net debt to GDP ratio remained the same because the net debt increased. The Province's net debt is approaching \$1.2 billion which is significant given the small population of the Province. This is reflected in an increase in taxpayer-supported net debt per capita.

**1.3** The Province incurred a deficit of \$83.8 million in 2002-03, the third consecutive year with a deficit. In addition, a deficit is projected for 2003-04. These recurring deficits indicate Government is spending beyond its means and will result in a higher debt load to service in the future.

**1.4** The 2002-03 deficit demonstrates the difficulty in controlling the Province's finances. Our vulnerability to Federal revenue was exposed with the reduction in federal revenue of \$66 million, the first substantial reduction in a number of years. Expenditures of the Department of Health and Social Services have increased by approximately 10 percent in each of the last two years. Due to demands on the health system these expenditures are difficult to

## 1. The Province's Finances

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control. The actual annual dollar increase of \$30 to \$40 million is significant in relation to the Province's budget.

**1.5** With the projected deficit for 2003-04, major challenges will continue in managing the Province's finances. On a positive note, new debt issues can currently be secured for long terms at relatively low interest rates; the Province is increasingly relying on its own sources of revenue; and the economy has expanded.

### BACKGROUND

**1.6** The Public Accounts record the government's financial activities in accordance with the recommendations of the Canadian Institute of Chartered Accountants. The statements combine the financial activities of many diverse government programs and entities with total expenditures of over \$1 billion.

**1.7** As in previous years, we are providing information to help put the numbers into perspective. The presentation is made in a format that focuses on key information to assist the Legislature and the public in obtaining a better understanding of the Province's financial condition. The Province's finances have a significant impact on the Provincial economy. It is essential that Members of the Legislature are provided with information to enable them to understand and debate the financial affairs of the Province.

**1.8** This discussion of the Province's finances is based on the Consolidated (Summary) Financial Statements, which include departments, the Special Projects Fund, Crown corporations, regional health authorities, school boards, and other organizations which are part of the overall government reporting entity.

## 1. The Province's Finances

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### FINANCIAL MEASURES

**1.9** Some of the common terms used to describe the Province's financial condition are presented below.

**1.10** The **annual surplus or deficit** is the difference between a government's revenues and expenditures. This measure shows the extent to which revenues raised in the year were sufficient to meet expenditures in that year. For the year ended March 31, 2003, the Province incurred a deficit of \$83.8 million.

**1.11** The **total debt** is the amount owed by the government. Government's debt includes outstanding debentures, pension obligations, and other accounts payable. The total debt of the Province as of March 31, 2003 was \$1.9 billion.

**1.12** **Financial assets** are cash and other assets which could provide resources to pay liabilities or finance future operations. Total financial assets at March 31, 2003 were \$732 million.

**1.13** The **net debt** is equal to the difference between the government's total liabilities and its financial assets. The net debt of the Province as of March 31, 2003 was \$1.166 billion.

**1.14** The **interest charged on borrowings** is the amount required to service the debt and must be taken from revenues before any expenditures can be made on government programs.

**1.15** The **gross domestic product (GDP)** is a measure of the value of the goods and services produced in the Province in a year. The Province's GDP is measured and reported by Statistics Canada.

**1.16** **Exhibit 1.1** shows a summary of some key financial measures for the Province over the past five years.

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## 1. The Province's Finances

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### EXHIBIT 1.1 PROVINCE OF PRINCE EDWARD ISLAND SUMMARY FINANCIAL INFORMATION (Millions)

	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>
Surplus (Deficit)	<b>\$ (83.8)</b>	\$ (37.3)	\$ (34.9)	\$ 12.4	\$ 28.1
Net Debt	<b>1,165.9</b>	1082.1	1044.8	1009.9	993.8
Debt Charges	<b>103.1</b>	107.1	107.8	102.7	101.4
GDP	<b>3,748</b>	3,474	3,349	3,159	2,981

**1.17** Over the past few years we have reported on certain key indicators of government's finances. These have been defined in the Research Report entitled, *Indicators of Government Financial Condition* published by the Canadian Institute of Chartered Accountants. The indicators are categorized as sustainability, flexibility and vulnerability. The trends in these indicators provide useful information to assess the financial condition of the Province.

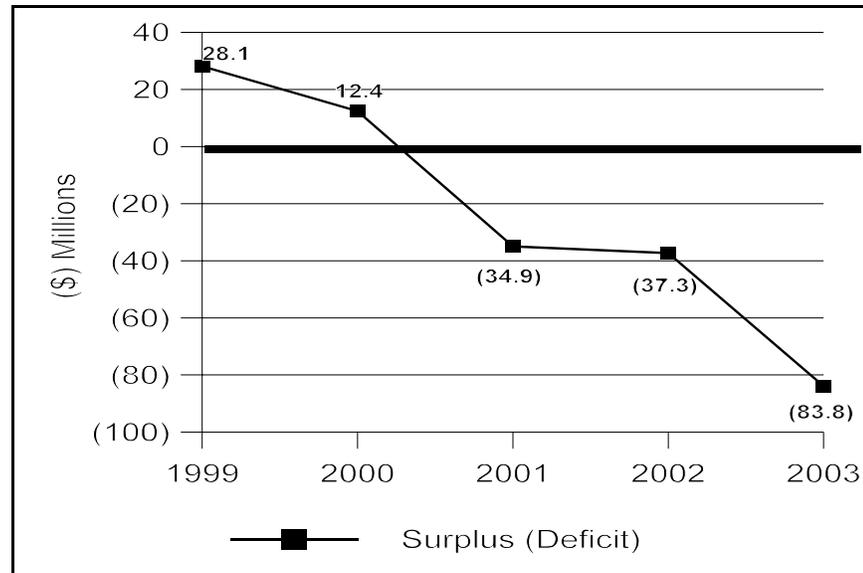
#### **Sustainability**

**1.18** Sustainability indicates whether the Province can maintain programs and meet existing creditor requirements without increasing the debt burden on the economy. A comparison of the government's annual surplus or deficit, net debt and the Provincial GDP provides insight into the sustainability of a government's practices of incurring expenditures and generating revenues.

**1.19** The annual deficit or surplus indicates the extent to which a government spends more or less than what it raised in revenue in a particular year. It basically shows whether Government is living within its means. **Exhibit 1.2** shows the annual surplus or deficit for each of the past five years. For the previous three years the deficits have totalled \$156 million. To reverse this trend government has to either increase revenue or reduce expenditures. A portion of the 2002-03 deficit is caused by day to day operational activities rather than one time capital projects. In terms of an individual this would be the same as borrowing money to purchase groceries.

## 1. The Province's Finances

### EXHIBIT 1.2 THE GOVERNMENT'S ANNUAL SURPLUS/DEFICIT



**1.20** The net debt is the difference between Government's total liabilities and its financial assets. Since 1999 the net debt increased by \$172.1 million or 17 percent and totalled \$1.166 billion at March 31, 2003.

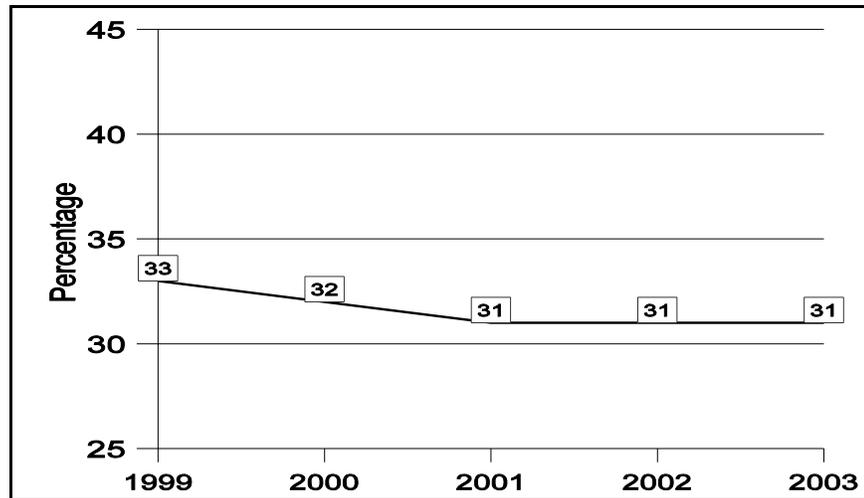
**1.21** The GDP of the Province indicates the size of our economy. The Province's economy supports government operations through taxes and fees. Prince Edward Island has experienced steady growth in the economy in recent years. While the net debt has increased by 17 percent since 1999, the GDP of the Province increased by 26 percent. Over the same period the GDP for Canada also increased by 26 percent.

**1.22** Exhibit 1.3 shows the net debt to GDP ratios since 1999. Even though, in 2002-03, the Province incurred a deficit of \$83.8 million and the net debt increased, the economy has continued to grow and the net debt to GDP ratio has remained steady. It should be noted that the percentage has remained the same for the last three years. Prior to that the percentage had been decreasing from a 1994 high of 41 percent.

## 1. The Province's Finances

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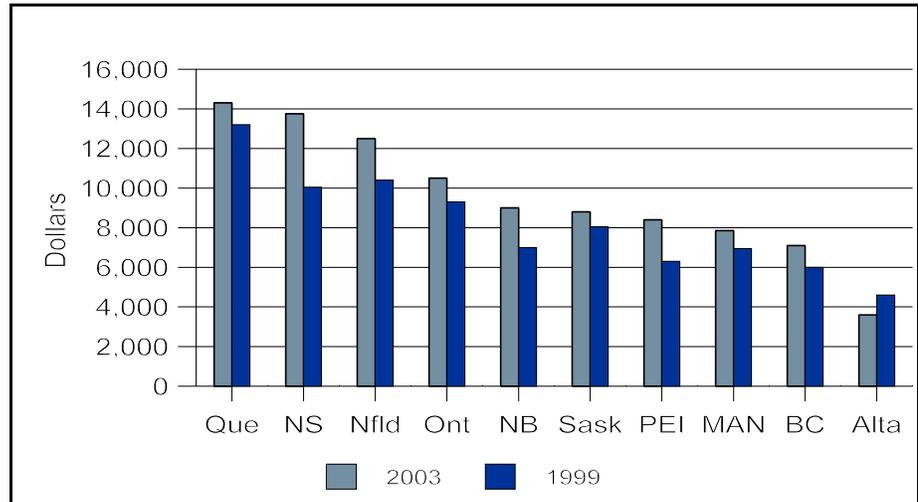
**EXHIBIT 1.3**  
**NET DEBT AS A PERCENT OF GDP**



**1.23** To help put this information into perspective, it is useful to compare our net debt per capita with other provinces. The Ministry of Finance for British Columbia reported the information in **Exhibit 1.4** for the fiscal years 2002-03 and 1998-99. The information is adjusted for interprovincial comparison and is presented on a different basis than our Public Accounts. However, it does provide a basis for assessment relative to the other provinces. It shows that as of March 31, 2003 the Province had the fourth lowest net debt per capita in the country compared to the third lowest at March 31, 1999. Based on the information in the Exhibit, PEI had the second highest percentage increase in net debt per capita over this period.

## 1. The Province's Finances

### EXHIBIT 1.4 INTERPROVINCIAL COMPARISON OF TAXPAYER-SUPPORTED NET DEBT PER CAPITA AS AT MARCH 31, 2003\* AND MARCH 31, 1999\*



\* Source: Moody's Investor Service

### Flexibility

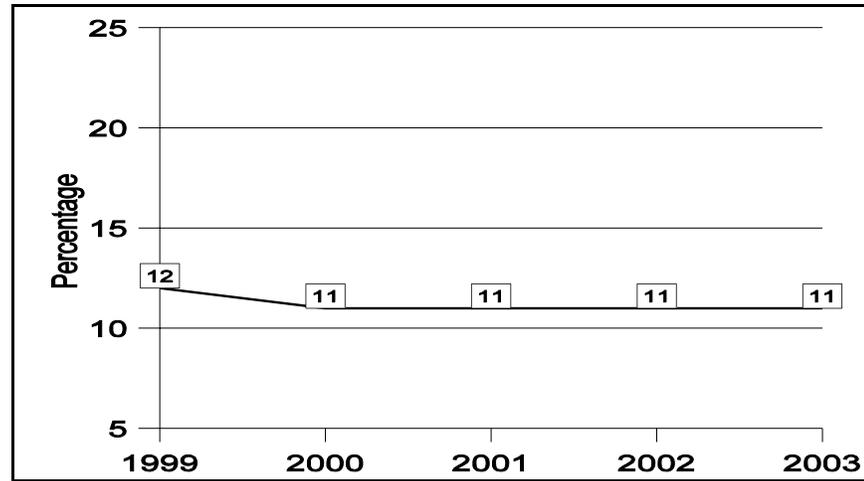
**1.24** Government's flexibility is the degree to which it can increase its financial resources to respond to rising commitments by either expanding its revenues or increasing its debt. A government meets the test of flexibility when it can respond to changing economic conditions such as a recession or higher interest rates without making substantial changes to the way it operates.

**1.25** A government's net debt and debt charges provide insight into whether it can respond to rising commitments without increasing its revenues. A rising debt burden and debt charges indicate there are fewer resources to allocate to programs and services. In the current year, the debt burden increased and debt charges decreased slightly.

**1.26** One measure of a government's flexibility is the interest costs as a percentage of total revenues. This is sometimes referred to as the "interest bite". In 2002-03, debt charges on government borrowings were \$103.1 million. The trend in the interest bite is shown in **Exhibit 1.5**.

## 1. The Province's Finances

### EXHIBIT 1.5 INTEREST COSTS AS A PERCENT OF REVENUE



**1.27** As indicated in **Exhibit 1.5**, the interest bite has declined from 12 percent in 1998-99 and is 11 percent for the current year. Our net debt is over a billion dollars and the first \$103.1 million must be earmarked to pay interest costs and is unavailable for government programs. Recent debenture issues have been for terms of 25-30 years at comparatively low interest rates.

**1.28** The total amount of interest expense for pension and other related obligations was \$15.3 million for 2002-03. As in previous years this amount was not included in debt charges.

#### Vulnerability

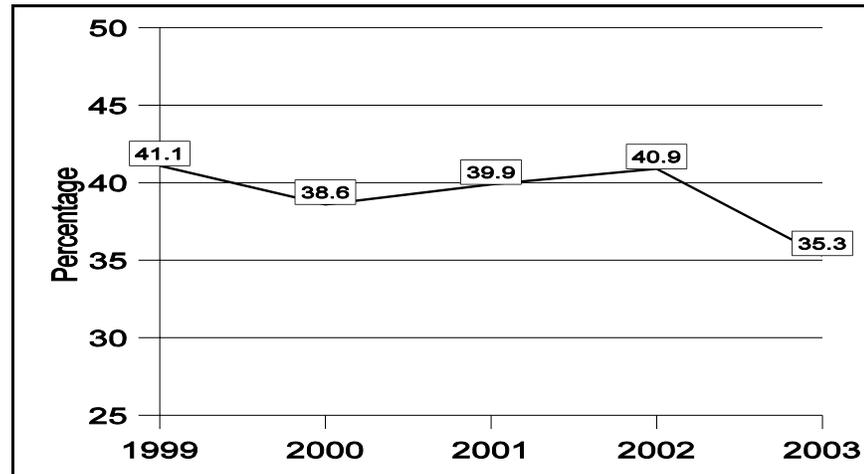
**1.29** Vulnerability is the degree to which a government is dependent on, and therefore vulnerable to sources of funding outside its control or influence. In 2002-03, the federal government provided approximately \$345 million to the Province, a decrease of \$66 million from 2001-02. In 2002-03 federal source revenues were \$15 million less than in 1998-99, a 4 percent decrease. This compares to provincial revenues which were 23 percent or \$117 million higher in 2002-03 compared to 1998-99. The trend in federal revenues relative to total revenues for the last five years is shown in **Exhibit 1.6**. This exhibit shows that approximately 35 cents of each dollar of revenue

## 1. The Province's Finances

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received by the Province in 2002-03 came from the federal government.

**EXHIBIT 1.6**  
**FEDERAL REVENUE AS A PERCENT OF TOTAL REVENUE**



**1.30** Revenue from provincial sources is more controllable through measures such as Provincial tax legislation or adjustments in user fees. Federal transfers are subject to different variables such as federal fiscal policies and the performance of other provincial economies. Any federal fiscal policy change impacts on the Province.

### SUMMARY

**1.31** It is important for Members of the Legislative Assembly to have a regular update on the financial condition of Government. This section provides summary information using indicators recommended by the Canadian Institute of Chartered Accountants. The indicators provide useful insight into government's ability to sustain its programs, the flexibility it has to respond to economic changes, and its vulnerability to sources of outside funding. The indicators help to put the finances of government into perspective and assist Members to understand and interpret the information.

## 1. The Province's Finances

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**1.32** Further to the above discussion, we recognize that there are other relevant non-financial matters which have to be taken into consideration by Members of the Legislative Assembly in making budgetary decisions and setting government policy direction.

**1.33** In the past we have posed some questions to stimulate debate in the Legislature. Given the current fiscal issues facing the Province it may be useful to revisit them. The questions are still relevant and are as follows:

- What is the optimum level of debt given our tax base and the level of services required?
- What level of debt is tolerable to our creditors?
- What portion of the budget are we willing to pay out in interest charges at the expense of productive program expenditures?
- What impact will changes to federal transfers have?
- What criteria should be used to determine the most appropriate steps to control and reduce the debt?
- What financial targets should be set and over what time frame?

# **SPECIAL AUDITS AND EXAMINATIONS**



## **2. INTRODUCTION TO SPECIAL AUDITS AND EXAMINATIONS**

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### **AUDIT PROCESS**

**2.1** Subsection 13(2) of the Audit Act states that the Auditor General may conduct any audit or examination he considers necessary to determine whether any agency of government is achieving its purpose, is doing so economically and efficiently and is complying with the applicable statutory provisions.

**2.2** Given the size of the Office and the complexity and size of government operations, it is not possible to audit all Government programs each year. In determining the annual audit program for the Office many factors are considered such as the results of previous audits, the total revenues and expenditures at risk, the complexity of operations, the significance of potential issues that may be identified by an audit, and the impact of the program on the public.

**2.3** Special audits and examinations are conducted in accordance with standards established by the Canadian Institute of Chartered Accountants. These types of audits are conducted in a series of stages. During the planning phase information is gathered to gain an understanding of the program or entity, and an audit plan is prepared. Evidence is obtained and analyzed and observations and recommendations are developed in the implementation phase. In the reporting phase a draft report is issued to the auditee for discussion. At the conclusion of the audit, a final report is issued to the department or agency and a written response is requested.

**2.4** Our work involves providing recommendations to management to address problems identified. We do not however infringe on management's right to select the most appropriate course of action to deal with the problems identified. We are primarily concerned that the issues raised are satisfactorily addressed.

**2.5** Under Section 16 of the Audit Act, the Auditor General is required to call attention to any matters which he considers necessary to be brought to the attention of the Legislative Assembly. This report provides information on the following: Crown Corporations-Control

## **2. Introduction of Special Audits and Examinations**

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and Accountability; Information Technology Security Review; Construction of the Atlantic Technology Centre; Government Garages; Water Management Division; and Federal Claims.

### 3. CROWN AGENCIES - CONTROL AND ACCOUNTABILITY

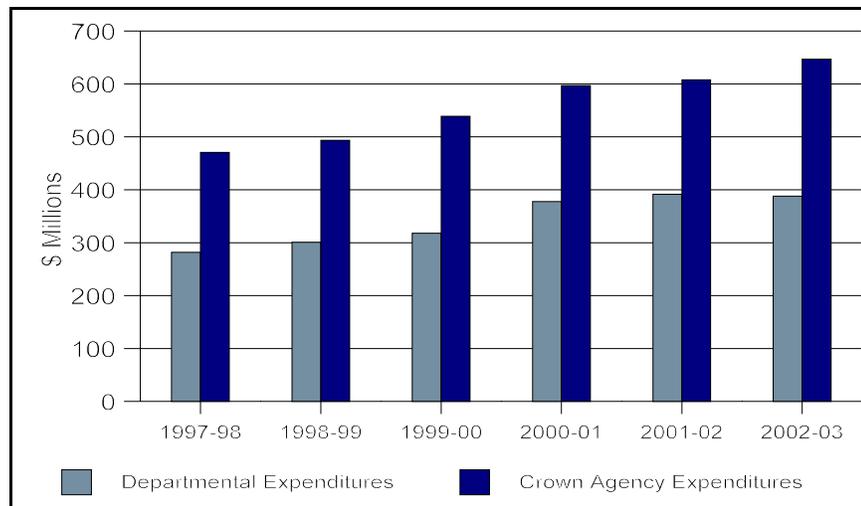
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#### BACKGROUND

**3.1** Crown agencies are distinct legal entities which are owned by government. They are established to deliver public programs and services and operate in many sectors of the Provincial economy including health, education, culture, agriculture, fisheries and technology. While there are many types of Crown agencies referred to as boards, commissions, corporations, and authorities, for the purposes of this report we refer to all as Crown agencies.

**3.2** Crown agencies vary widely in size, in the extent of financial resources they receive from government, and in the level of autonomy of their operations from the related government departments. The total expenditures of Crown agencies are substantial compared to those of government departments as illustrated in **Exhibit 3.1**. Since 1997-98, expenditures of both departments and Crown agencies have experienced significant growth.

**EXHIBIT 3.1**  
**GOVERNMENT EXPENDITURES BY DEPARTMENTS**  
**AND CROWN AGENCIES**



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### **3. Crown Agencies - Control and Accountability**

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**3.3** While Crown agencies provide an opportunity to achieve public policy and other goals and to generate revenue, they also represent significant exposure to potential financial losses and other risks. The Crown agencies listed in the Schedules to the Financial Administration Act had total debt obligations (amounts payable to the Province and to the private sector) at March 31, 2003 of \$367 million. Government budgetary appropriations for these agencies are approximately \$500 million annually.

**3.4** Crown agencies, as separate legal entities, are each administered in some manner by a board of directors and have more management autonomy than government departments. Distinct relationships exist between the board of directors of the Crown agency, the Minister responsible, the government and the Legislature. There is clearly a balance to be struck between the “arm’s length” operations of a Crown agency and the appropriate level of direction and control to be exercised by government in representing the interests of taxpayers.

**3.5** In general, Crown agencies operate within a set of parameters which, when taken together, establish a framework for oversight. The primary legislation is the Financial Administration Act which defines Crown corporations and reporting entities and identifies, in its schedules, those subject to its legislative requirements. It sets out minimum reporting requirements such as budget information, audited financial statements, and annual reports. Many Crown agencies are established under individual Acts which set out other specific requirements for their operation and establish their mandate. Treasury Board policies have also been developed, some of which are applicable to Crown agencies.

**3.6** In any accountability relationship it is essential that the parties understand the responsibility conferred and reach agreement on how the discharge of that responsibility will be demonstrated. In the case of Crown agencies the acknowledgement of a minimum set of requirements is critical. The nature of Crown agencies means that there will be a wide variation in the mandates and objectives they will be charged with, as well as very diverse environments within which they will operate. The acceptance of minimum accountability

### **3. Crown Agencies - Control and Accountability**

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requirements assists both the board of directors and legislators. The first in ensuring the work of the Crown agency is focused on the priorities of government and the second in providing a body of information, presented in a consistent manner, which allows for informed discussion and debate.

#### **OBJECTIVES AND SCOPE**

**3.7** In accordance with Section 13 of the Audit Act, we conducted an examination of control and accountability of Crown agencies. Our objective was to review governance, accountability and reporting in accordance with legislation, policy and government practices. Our review covered all Crown agencies as listed in Schedules B, C, and D of the Financial Administration Act.

**3.8** Our examination was performed in accordance with the value for money auditing standards of the Canadian Institute of Chartered Accountants (CICA) and accordingly included such tests and other procedures as we considered necessary in the circumstances.

**3.9** For each agency we reviewed the enabling legislation or incorporating documents, financial information, annual reports and related documents. Further, we interviewed a number of CEOs and board Chairs with respect to governance and accountability issues. We also reviewed legislation and a number of policies in the federal government and several provinces.

#### **DETAILED AUDIT OBSERVATIONS**

##### **Governance**

**3.10** Corporate governance describes the process and structure for overseeing the direction and management of a corporation so that it effectively fulfils its mandate. Crown agencies have greater managerial autonomy than departments. The accountability framework that is established is designed to balance this autonomy with accountability to both the government and the Legislature.

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### 3. Crown Agencies - Control and Accountability

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**3.11** The majority of Crown agencies are created through an Act of the Legislature. These Acts set out the requirements for a board of directors and state any specifications regarding the appointments to the board. A board of directors oversees the direction of the Crown agency and holds management accountable for the agency's performance. Generally, the board, through the chair, is accountable to the Minister responsible. The Minister responsible provides the link between the Crown agency and both Executive Council and the Legislature.

#### *Appointments to the Board*

**3.12** The appointment of board members is addressed within the enabling legislation or articles of incorporation of each Crown agency. In several cases the board members are elected, but in most cases they are appointed either by the Lieutenant Governor in Council or the Minister. Policy and procedures have been developed by the Executive Council office to assist departments and agencies in carrying out their responsibilities related to appointments to boards of Crown agencies. This policy provides that the process for appointment will include presenting the names to Executive Council for approval.

**3.13** In many of the pieces of enabling legislation the appointment term is specified which in most cases is a three year term. We noted the policy set by Executive Council indicates a desire to limit appointments going forward to a maximum of two terms. This is to encourage the ongoing renewal and energy of the boards and to allow increased citizen participation.

**3.14** We noted the size of the boards of directors of Crown agencies varied from 1 to 13 members. While there is no one board configuration that is preferable to any other, the primary consideration must be the ability of the board to effectively fulfil its responsibilities.

**3.15** In the case of the Provincial Health Services Authority (PHSA), the CEO is appointed as the sole board member. This governance structure is very unusual and essentially establishes a Crown agency without a board of directors but rather with a CEO reporting to the Minister. A director is expected to exercise the care, due diligence and

### 3. Crown Agencies - Control and Accountability

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skill of a reasonably prudent person and apply good business judgement based on common sense and his or her personal experience. The fulfilment of the responsibilities of the board assumes the presence of not one board member but rather several board members, who together bring to bear their separate knowledge and experience on the issues and responsibilities facing the board.

**3.16** The PHSA has been set up through legislation as a separate Crown agency. It has an annual budget of \$110 million and responsibility for planning and delivering specialized acute and secondary health care to all Islanders. This agency is a large and complex organization similar to the regional health authorities each of which has a full board as well as a separate CEO. The magnitude and impact of the operations of this Crown agency clearly demonstrates the need for a fully constituted board of directors.

#### **Recommendation**

**3.17 The governance structure for the Provincial Health Services Authority should be revised and brought in line with similar Crown agencies in the public sector.**

#### *Board Skills*

**3.18** We did not review the qualifications of specific board members, nor did we have any indication of problems in this regard. However, as the magnitude and complexity of these corporations increase, and the business environments in which they operate become more global, it may be more desirable than ever before to attract certain skill sets to boards of Crown agencies. Some legislation specifies requirements, for example, for board members to represent certain economic sectors, while other pieces of legislation are silent on board qualifications. We would not recommend entrenching a skills set requirement within the legislation, however, the need for certain qualifications and experience at the board table should be considered and documented.

### 3. Crown Agencies - Control and Accountability

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#### Recommendation

**3.19 Each Crown agency board should develop and document guidelines on the desirable qualifications and attributes of prospective board members.**

#### *Management and Board Relationship*

**3.20** In private sector corporations the CEO is appointed by the board of directors and is responsible to it. By virtue of the board's authority to evaluate the performance of the CEO and take decisive action, there is no question of where the CEO's accountability lies.

**3.21** For the majority of Crown agencies, the CEO is appointed by Executive Council. The role of the board of directors in the recruitment and selection of the CEO can vary. This practice gives rise to a dual accountability on the part of CEOs to both the board of directors and the Minister responsible. While this may be workable, it complicates the environment within which the CEO must function.

**3.22** The nature of the relationship between the board of directors and management of the corporation is critical. The board normally delegates its responsibilities for management of the business and affairs of the corporation to the CEO. The board does not normally participate in the day to day operations but concerns itself more with setting the long-term direction and objectives of the corporation and monitoring the performance of both the CEO and the corporation overall.

**3.23** We interviewed ten CEOs of the larger Crown agencies regarding their relationships with their respective boards of directors. Most acknowledged a dual accountability to both the Minister and the board but indicated it had not caused problems. Four of the ten CEOs indicated there was no formal review of their performance conducted by the board.

**3.24** In two of the Crown agencies, Island Regulatory and Appeals Commission (IRAC) and PHSA, we noted that the CEO was also the chair of the agency board. In Tourism PEI, both the CEO and Director

### 3. Crown Agencies - Control and Accountability

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of Finance are named as directors to the board. In these situations there is no separation between the board and management of the corporation. It is difficult for the board to hold management accountable for their performance. The board cannot function as intended, providing direction and oversight to the corporation and acting independently from management.

#### **Recommendation**

**3.25 Each CEO should have a formal performance evaluation conducted by the board of directors on a periodic basis.**

#### *Board Responsibilities*

**3.26** To fulfil their responsibility to manage the affairs of the corporation, boards of directors exercise judgement in four broad areas:

- establishing the corporation's strategic direction;
- safeguarding the corporation's resources;
- monitoring corporate performance; and
- reporting to government and the Legislature.

**3.27** We did not review minutes of the board meetings of all Crown agencies. However, we did interview CEOs of ten of the larger Crown agencies and asked specific questions regarding the functioning of the board of directors. We noted in two of the ten Crown agencies that the board was not meeting on a regular basis.

**3.28** Government tourism related activities are delivered through a Crown agency known as Tourism PEI which has an annual budget of approximately \$18 million. The board of Tourism PEI consists of the Minister who is chair, the Deputy Minister who is CEO of the corporation, the Director of Finance and two private sector representatives. We noted for at least the past two years the board has held only one meeting per year in the month of June. We were advised that the board did not approve the strategic plan, the annual report, or the budget and that the entity in effect operates like a department.

### 3. Crown Agencies - Control and Accountability

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**3.29** The PEI Business Development Inc. Act was proclaimed in November of 1999. During the course of audit work in 2001 and again in 2002 we noted that the board was meeting infrequently and we recommended that the board fulfil its responsibilities as stated in the Act. This year we noted that the board was inactive during the past year. We have recently been advised that a new board of directors has been appointed which met for the first time in November 2003. PEI Business Development Inc. is a Crown agency with annual expenditures of approximately \$35 million, that delivers a diverse set of programs and development initiatives, and administers nine subsidiaries and one subsidiary of a subsidiary.

**3.30** In addition to the responsibilities of boards as governing bodies there are also responsibilities required of individual board members as directors. The Federal Financial Administration Act clearly defines the duties and responsibilities of directors to act honestly and in good faith, exercise care, diligence, and skill, and uphold the charter and by-laws of the corporation. Individual directors should be aware of their general responsibilities and, for example, where the board is not meeting, they should consider the impact on their ability to fulfil their responsibilities as directors.

**3.31** We determined from our interviews with CEOs that, with the exception of the two Crown agencies referred to above where the boards were not meeting, the boards of the Crown agencies normally receive some form of interim financial reports. In the case of Tourism PEI and BDI, corporate plans and budgets were prepared but did not receive formal board approval.

#### **Recommendation**

**3.32** Boards of directors should fulfil the responsibilities as set out in the enabling legislation of the Crown agency as well as the general responsibilities of corporate directors.

#### *Audit Committees*

**3.33** An audit committee is a core committee of a corporation's board of directors. The audit committee fulfils a significant role in

### 3. Crown Agencies - Control and Accountability

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addressing and monitoring key financial and performance information and assists in more clearly delineating the role of the board from that of management.

**3.34** Audit committees' general responsibilities include reviewing interim and annual financial statements, obtaining information concerning risks and exposure, and meeting with the external auditor independent of management. The Federal Financial Administration Act requires that parent federal Crown corporations establish an audit committee. In addition recent recommendations of the Canadian Institute of Chartered Accountants require the auditor to communicate with the corporation's audit committee.

**3.35** Based on our interviews with ten CEOs, only one of the Crown agencies had an audit committee established. Where audit committees are not in place the onus is on the board of directors to ensure the responsibilities normally met through the audit committee are carried out by the board.

#### **Recommendation**

**3.36** An audit committee should be appointed for each Crown agency or, where not appointed due to size, the board of directors should carry out the responsibility.

#### *Governance Policies*

**3.37** In reviewing information on 31 Crown agencies as well as conducting interviews with CEOs of ten of the larger Crown agencies, we noted significant differences in the governance structure and processes within these organizations. We acknowledge that each of these entities has been created for a unique purpose and a certain amount of flexibility is required for each to fulfil its own mandate and objectives. However, it is appropriate for all Crown entities to follow minimum good governance practices.

**3.38** We have made a number of recommendations on governance issues. It is important for Treasury Board to establish guidance on governance expectations within the Public Sector. Treasury Board

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### 3. Crown Agencies - Control and Accountability

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Secretariat of Canada has developed guidelines designed to strengthen the effectiveness of boards of directors in the federal public sector and these guidelines may provide valuable input to the development of provincial guidance.

#### **Recommendation**

**3.39 Treasury Board should develop requirements for corporate governance applicable to all Crown agencies.**

#### **Framework for Accountability**

**3.40** Crown agencies are delegated responsibility by government for programs and services, and are expected to report back to government on their performance at various levels. This reporting is a fundamental aspect of accountability. In the case of Crown agencies, the agency must demonstrate responsibility for performance of results relative to agreed upon goals and resources used. Important tools in the accountability process include plans, budgets, financial statements and annual reports.

#### *Crown Agencies' Roles*

**3.41** The general roles of the 31 Crown agencies are defined in their enabling legislation or Articles of Incorporation. All of the agencies we examined had formal purposes, objects, functions, powers, duties, responsibilities and/or other forms of mandate defined.

**3.42** Each Crown agency was established to meet public policy objectives and a decision was made to deliver the programs or services outside departmental operations. It is realistic to expect that the nature of the operations of these agencies may change over time and their role and governance structure may require periodic review. For example, the PEI Housing Corporation and the PEI Crown Building Corporation have a long list of objects, some of which they are not performing. These corporations are largely inactive except for holding property and/or financing. The roles of these agencies have changed over time and require review, in light of government's current vision.

### 3. Crown Agencies - Control and Accountability

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#### Recommendation

**3.43 The purpose and objects of Crown agencies should be reviewed periodically to determine whether the agencies are of ongoing need and reflect the current intentions of government.**

#### *Corporate Plans*

**3.44** Each Crown agency has a key role in interpreting its mandate as set out in legislation. The board of directors of each Crown agency must approve the corporate objectives and the strategies to achieve them while balancing its public policy and other responsibilities. These considerations are normally documented in a corporate plan. The corporate plan is the cornerstone of the accountability framework for Crown agencies.

**3.45** In PEI there is no formal requirement for Crown agencies to prepare a complete corporate plan. However, 21 of the 31 agencies we examined had some form of strategic, business or operating plan. We did not assess the quality of the plans provided. We noted that only a few of the plans were available as public documents.

**3.46** The approval of corporate plans by government assists in clarifying government's endorsement of priorities identified and the strategies being followed by the Crown agency. This approval at the planning stage provides the basis for accountability reporting based on agreed upon objectives and targets. In general we found that most Crown agencies had some form of planning process in place. However, there was no process for consistent review and endorsement of Crown agency plans by government.

#### Recommendation

**3.47 Executive Council should establish a corporate planning process for all Crown agencies which includes at least the following:**

- a corporate plan approved by the board of directors;
- endorsement by the Minister responsible;

### 3. Crown Agencies - Control and Accountability

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- review and approval by Treasury Board and/or Executive Council;
- release to the Legislative Assembly in conjunction with the budget approval process; and
- linkage to the corporate annual report.

#### *Budget Estimates Presentation*

**3.48** The Budget Estimates is the core financial planning document which provides information on government's projected expenditures for the coming year. The information presented in the Budget Estimates provides the basis for review and debate within the Legislature. The amounts presented in the Budget Estimates are listed in the Appropriation Act which is approved by vote in the Legislature. The approved appropriation is the maximum expenditure allowed for that department or agency except in the case where a special warrant is approved by Executive Council. Within each appropriation vote transfers may be made. Because the Appropriation Act is the spending authority of government, transfers may not normally be made from one appropriation vote to another.

**3.49** Not all Crown agencies require an annual appropriation. Some, like the PEI Liquor Control Commission are net revenue generating organizations. Of the 19 Crown agencies which had a budgeted appropriation for the 2003-04 fiscal year, 7 had a separate appropriation vote. The remaining 12 entities were included in the appropriation vote of their respective department. There did not appear to be any specific rationale as to why some Crown agencies are included under the related department vote and others are not. For example, in the case of regulatory type entities, IRAC has its own appropriation vote while the Human Rights Commission is included with the Attorney General's Office. Entities requiring small appropriations, such as the PEI Grain Elevators with an appropriation of \$165,000, had a separate vote while large agencies like the regional health authorities were included in the appropriation for the department.

### 3. Crown Agencies - Control and Accountability

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**3.50** The Budget Estimates provides the information which supports the spending approval for government and allows discussion and debate prior to the appropriation votes. We noted major inconsistencies in the presentation of budget information for Crown agencies.

**3.51** The budget information for many agencies is presented as a one line grant or a grant that covers a portion of the agency's expenditures. An example is the PEI Lending Agency which receives funding for salaries and administration. The complete expenditures budget for this organization is not presented in the Budget Estimates document. Instead, only the expenditures that will be funded by the provincial grant are presented.

**3.52** A number of Crown agencies have budgets providing detail similar to a Department, but even within this group the amount of information varies considerably. The regional health authorities and school boards are budgeted by type of expenditure on a consolidated basis such that each program includes all regions or boards. Budgets for individual school boards and regional health authorities are not included in the Budget Estimates in spite of the fact that they are separate legal entities each with its own board of directors.

**3.53** Budget Estimates presentation is inconsistent in some entities as it relates to revenue. For example, in the case of the health authorities, hospital revenues which are collected by the authority are netted against other expenditures whereas other revenues are deposited directly to the Province and presented as general provincial revenue.

**3.54** In other cases agencies receive funding which is not readily identifiable within the Budget Estimates because it is considered program funding. This includes crop insurance and operations-related costs of the PEI Agricultural Insurance Corporation. The above funding is included within the budget of the related department under various programs. Even though the PEI Agricultural Insurance Corporation is a separate Crown agency and has financial statements included in the public accounts, there is no identifiable budget in the Budget Estimates.

### 3. Crown Agencies - Control and Accountability

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**3.55** The Public Accounts for the Province provides the detailed financial results of government. The consolidated financial statements provide the combined results of departments and Crown agencies except for the Workers Compensation Board. In addition, with the exception of the Employment Development Agency, the separate audited financial statements of each Crown agency are published in the Public Accounts, Volume II. These financial statements include the overall financial results, but not budget information sufficient for comparison with approved appropriations.

**3.56** The information provided in the Budget Estimates is often insufficient to assess the overall financial plan for the organization. Financial statements typically include a comparison of actual financial results with the previous year but do not provide information on actual results compared to the appropriations approved by the Legislature. Comparing budget information for most Crown agencies to the actual financial results is difficult with the current budget presentation.

#### **Recommendations**

**3.57** The Appropriation Act should be reviewed for consistency with respect to agency size and accountability.

**3.58** Information provided to the Legislature for Crown agencies should include budgets showing revenues and expenditures of the agency and its subsidiaries, arriving at a net revenue item or net appropriation required.

**3.59** In addition to budgets by program area for health authorities and school boards, the Budget Estimates should at a minimum provide supplementary information showing budgeted revenues and expenditures by health authority and school board.

#### **Subsidiaries**

**3.60** Subsidiary companies are created as separate legal entities for a legal or administrative purpose. For example, the Provincial golf courses were previously run within the Department of Tourism until

### 3. Crown Agencies - Control and Accountability

the operation was transferred to a subsidiary of Tourism PEI, Golf Links PEI Inc. This provided increased operating and financial autonomy. At the time of this report, there were 20 subsidiaries as listed in **Exhibit 3.2**. Some of the subsidiaries, such as Technology PEI Inc., are large organizations which can present greater risk than some parent Crown agencies due to the increased autonomy of subsidiary operations.

#### EXHIBIT 3.2 CROWN AGENCIES AND SUBSIDIARIES AS AT MARCH 31, 2003

Ministry	Crown Agency	Subsidiary	Subsidiary of a Subsidiary
Development and Technology	PEI Business Development Inc.	Corporate Services Ltd. Environmental Industrial Serv. Inc. FTC Enterprises Ltd. Island Products Holdings Inc. Souris Food Park Develop. Corp. Solatum PEI - A Canadian Potato Systems Company Inc. Technology PEI Inc. 100417 PEI Inc. Gateway Village Development Inc.	ATC Inc.
	PEI Energy Corp.	Atlantic Wind Test Site Inc.	
	Charlottetown Area Development Corp.	Harbourside Complex Limited The Charlottetown Waterfront Development Corporation	
	S'side Regional Development Corp.	Summerside Cultural Development Corporation Ltd.	
	Island Investment Development Inc.	PEI Gov't Econ. Dev. Fund #2 Inc. PEI Gov't Econ. Dev. Fund #3 Inc. PEI Gov't Econ. Dev. Fund #4 Inc. PEI Gov't Econ. Dev. Fund #5 Inc. PEI Century 2000 Fund Inc.	
Tourism	Tourism PEI	Golf Links PEI Inc.	

**3.61** Subsidiaries are formed by incorporating a company under the PEI Companies Act or the Canada Business Corporation Act. Unlike Crown corporations, subsidiaries are not approved through the Legislature, nor is there a specific requirement for subsidiary corporations to be established by Order in Council.

### 3. Crown Agencies - Control and Accountability

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**3.62** The Federal government has requirements for subsidiary corporations that are similar to those for parent corporations. These include Federal Cabinet approval for the creation and dissolution of subsidiaries, audited financial statements and annual reports. Reporting requirements may be met through the reports of the parent as long as there is adequate disclosure.

**3.63** We were advised that although in this Province there is no formal requirement for approval of subsidiaries through Order in Council, Executive Council is aware of their creation. The PEI Financial Administration Act and Treasury Board Policy apply only to parent Crown agencies. The financial results of the subsidiary corporations are included in the annual report of the parent. The extent of performance information available on subsidiary corporations varies greatly. For example, PEI Business Development Inc. has nine subsidiaries. The financial results of all are consolidated in the BDI audited financial statements. Two of these subsidiaries, the Food Technology Centre (FTC Enterprises Ltd.) and Technology PEI publish separate annual reports while the annual report of BDI does not specifically mention the results of some of the other subsidiaries such as Island Products Holdings Inc.

**3.64** In our view, subsidiary corporations should be accountable to the Legislative Assembly and the public for their performance and results. At a minimum the governance and accountability requirements should be considered when the corporation is created and the ongoing reporting of information on program performance and financial results should be presented either in a separate report or within the report of the parent company.

#### **Recommendations**

**3.65 The creation of subsidiaries should require formal approval by Executive Council and the governance and accountability structures should be clearly defined when the subsidiaries are created.**

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### 3. Crown Agencies - Control and Accountability

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**3.66 Treasury Board should establish standards for subsidiary corporations regarding reporting on program performance and financial results.**

#### Accountability Reporting

**3.67** Annual reports and financial statements are essential components of accountability reporting because they are the key performance documents available to the Legislature and the public. The Financial Administration Act sets out the requirements for annual reporting by government organizations in Section 70; requiring each reporting entity to submit an annual report including an audited financial statement and a statement of goals and results achieved. A reporting entity is defined in the Act as an organization that is accountable for the administration of its financial affairs and resources to a Minister or through a Minister to the Legislative Assembly and includes those listed in Schedules B, C and D of the Act.

**3.68** Along with the Act, a supporting Treasury Board Policy, Accountability and Governance Matters: Annual Reporting Framework, was approved to provide direction on the principles, content and process to be followed in the preparation and presentation of annual reports. The legislation and policy make accountability reporting, with a focus on goals and results achieved, a requirement for all government departments and Crown agencies.

**3.69** In addition to reviewing annual reports of Crown agencies for compliance with the legislative and policy requirements, we applied a framework adopted from work performed by the Auditors General of Canada and British Columbia. The framework includes eight key elements ranging from the strategic direction of the organization to important aspects of reporting on results. Each report was rated on a scale from start-up to fully developed in relation to these elements.

**3.70** While the requirements of the Financial Administration Act and Treasury Board Policy have been in place since 1996, most of the annual reports we examined were typically in the start-up stage of development in terms of presenting quality accountability information. The reports were strongest in the areas of being focused on critical

### 3. Crown Agencies - Control and Accountability

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aspects of performance and presenting comparative information. Comparative financial information was almost always presented. The reports were weaker in identifying clear goals and performance expectations, and comparing results with expectations.

#### *Strategic Direction and Goals*

**3.71** The primary function of an annual report is to be the main accountability document from Crown agencies to the Legislative Assembly and the public. It provides a link between the strategies and goals of the organization and the results achieved. Ideally the strategies and goals in the annual reports should flow from planning documents such as strategic and business plans. These plans should include approved goals and expected results for the period as an essential element of an accountability relationship.

**3.72** We looked for the annual report to contain enough of the organization's strategic direction and performance targets to allow the reader to determine what management set out to accomplish when the year began. The greatest weakness we observed in the annual reports we examined was an absence of measurable goals and/or objectives. Of the 27 reports we examined, most stated what they expected to achieve in general terms while only 5 included measurable goals or expected outcomes.

#### **Recommendation**

**3.73 Each annual report should provide clearly stated goals endorsed by the board of directors and the Minister Responsible.**

#### *Performance and Results Achieved*

**3.74** Once the goals are established, methods for measuring performance against the goals must be determined. Performance measures should be designed to compare actual performance to performance expected. The measures should also focus on the critical areas that best illustrate the progress made towards organizational goals. Ideally, these measures should track outcomes rather than the activities or outputs.

### 3. Crown Agencies - Control and Accountability

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**3.75** The Financial Administration Act requires annual reports to report on results achieved. Treasury Board Policy requires information on how performance is measured and a comparison of results achieved against expectations. Twenty-one of the 27 annual reports that we reviewed provided information on activities and accomplishments during the year, five provided information based on outcomes or results achieved, and one did not have any activities. Since goals were only expressed in measurable terms in a few cases, actual results could not be compared with expected results in most cases.

#### **Recommendation**

**3.76 Each annual report should demonstrate the relationship between the goals of the Crown agency, the activities carried out, and the results achieved.**

#### *Analysis of Results and Comparative Information*

**3.77** The results achieved by organizations will not necessarily be the same as planned. Many things may happen in the course of a year that lead to either positive or negative changes. Where significant changes occur relative to plans or past performance, the report should include management's analysis of the situation. Comparative and trend information can be useful in indicating changes but should be interpreted in the context of the business environment.

**3.78** All of the annual reports we examined provided some type of comparative information, usually in the financial statements. Several annual reports contained adequate analysis or discussion of results to support their performance relative to their strategic objectives.

**3.79** Treasury Board Policy calls for the annual reports to include both successes and failures in reporting on results achieved. Based on our review, the majority of annual reports included information on favourable performance but many did not include information on performance that did not meet expectations.

### 3. Crown Agencies - Control and Accountability

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#### Recommendation

**3.80 Annual reports should include an explanation for significant variances from expected performance, both favourable and unfavourable.**

#### *Timely Reporting*

**3.81** Section 70 of the Financial Administration Act requires that reporting entities prepare and release annual reports in a timely manner:

#### *The Minister shall...*

- (a) lay the report before the Legislative Assembly within fifteen days after he receives it or if the Legislative Assembly is not then in session within fifteen days after the commencement of the next ensuing session;*
- (b) make the report available to the general public as soon as possible but within six months of the end of the financial year whether or not the document has been laid before the Legislative Assembly.*

**3.82** All of the Crown agencies listed in Schedules B, C and D of the Financial Administration Act are subject to the requirements set out in Section 70. We noted, however, that four of these Crown agencies did not produce an annual report for the year ended March 31, 2002. These were Island Waste Management Corporation, the Special Projects Fund, Island Investment Development Inc., and the PEI Self-Insurance and Risk Management Fund.

**3.83** The requirement of the Financial Administration Act is that the reports be released within six months of the financial year-end of the organization. The Act requires the annual reports to be released to the public if the Legislature is not then in session, but also provides for the reports to be tabled when the Legislature subsequently sits. The Treasury Board Policy refers to the protocol for the release of annual

### 3. Crown Agencies - Control and Accountability

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reports when the Legislature is not in session. Strictly applying this time frame reveals that only three Crown agencies released their annual reports on time.

#### **Recommendation**

**3.84 Each Crown agency identified in the Financial Administration Act should provide an annual report within six months of its financial year end in accordance with the requirements of the Act.**

#### *Review of Annual Reports*

**3.85** The key performance information on the goals and achievement of results for each Crown agency is critical information for effective corporate management. However, the primary purpose of an annual report is to demonstrate accountability of the Crown agency to the Legislative Assembly and the public. Crown agencies will dedicate more effort to ensure that plans and reports are complete, accurate and credible if they know that the information they provide is being used for decision making or debate about the progress of the agency.

**3.86** If the Legislative Assembly is to assess the performance of government, it must be informed about what government intends to achieve and what it actually achieves. Simply tabling an annual report in the Legislature does not ensure it will be given the scrutiny it requires. The Legislative Committee system can be an effective structure for discussing the progress of Crown agencies. In some jurisdictions annual reports of Crown agencies are automatically referred to Standing Committees for review.

**3.87** At the time of our audit there were seven Legislative Committees. Four of these dealt with issues within certain Ministries or sectors and could be charged with the review of annual reports of Crown agencies within the purview of the associated Ministries.

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### 3. Crown Agencies - Control and Accountability

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**Recommendation**

**3.88 Annual reports of Crown agencies should be referred to a Standing Committee for review of agency performance.**

**MANAGEMENT RESPONSE**

**3.89** The report was issued to Executive Council. We were advised that it has been forwarded to the Provincial Treasurer for further analysis and follow-up.

## 4. INFORMATION TECHNOLOGY SECURITY REVIEW

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### BACKGROUND

**4.1** Government's electronic information systems are used to receive and store private and sensitive information about Islanders. The types of information collected on government information systems include everything from medical information about individuals to revenue information about businesses. Government has a responsibility to ensure the information is adequately protected. Information Technology (IT) Security is defined as the protection of systems and data from accidental and deliberate threats to confidentiality, integrity and availability. The potential threats to information stored on government computer systems would include:

- inappropriate use of confidential or private information;
- modification or damage to databases; and
- interruptions in service.

**4.2** The resources assigned to information technology are considerable. They include direct annual expenditures of approximately \$20 million and over 160 staff assigned to maintain and operate information technology systems.

**4.3** As part of our review we asked departments and agencies to respond to a security self-assessment questionnaire. In the overall assessment of the adequacy of security, on a scale of 1 to 10, with 10 being the most favourable assessment, departments ranked themselves on average at 5.7 and agencies ranked themselves at 6.8. Both rankings indicate that IT security needs to be given higher priority if the confidentiality and integrity of information is to be protected. The most frequently cited reasons for incomplete security controls were; budget constraints, controls not cost justified, and difficulty in hiring and retaining employees.

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## 4. Information Technology Security Review

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### OBJECTIVE AND SCOPE

**4.4** In accordance with Section 13 of the Audit Act, we conducted a review of Information Technology Security in departments and agencies. Our objective was to assess whether information stored and processed was adequately protected. We surveyed departments and agencies to obtain information on information technology security practices. The review also consisted of interviewing staff, examining documents and reviewing agreements.

### DETAILED OBSERVATIONS

#### Responsibility

**4.5** Treasury Board Policy outlines responsibilities for planning and management of information technology, including security. The Policy assigns responsibilities for: Treasury Board; the Information Management Advisory Council (IMAC); the Department of the Provincial Treasury; and other departments.

**4.6** Treasury Board approves policy and funding for IT activities. IMAC is responsible for providing strategic direction on IT within the public sector. Related to IT security, IMAC will:

- approve and maintain overall responsibility for IT security for Government, which includes establishing policies, directions and standards; and
- report to Treasury Board annually on the status of IT security within Government departments.

**4.7** IMAC responsibilities related to approving and maintaining overall IT security and reporting on the status of IT security to Treasury Board were not being addressed because IMAC was not operating. An IT Security Self-Assessment was conducted in October 2002 but was not presented to IMAC because IMAC was not operational at that time.

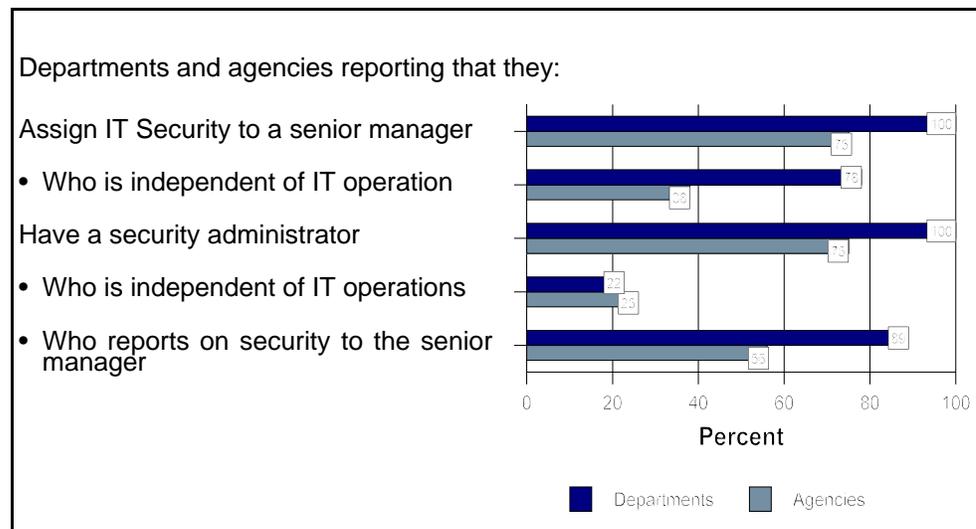
## 4. Information Technology Security Review

**4.8** Treasury Board has recently established an IT Governance Council to replace IMAC. The Council is expected to oversee information and communications technology policy, strategy and investment at a corporate level. The terms of reference which directly relate to IT security include:

- ensure risk associated with the application of information technology is managed at the appropriate level of the organization; and
- ensure the development of effective IT policies and standards across the organization.

**4.9** Within each department the Deputy Minister is responsible for IT security. Each department has also assigned an IT security coordinator to handle the daily activities. In response to our survey, all of the departments and 12 of 16 agencies surveyed indicated that a senior executive was assigned responsibility for IT security. A summary of survey results related to responsibility is shown in **Exhibit 4.1**. Although the IT coordinators were not usually independent of the operating functions of the systems, most of them reported directly to senior management on IT security related issues.

**EXHIBIT 4.1  
RESPONSIBILITY FOR SECURITY**



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## 4. Information Technology Security Review

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### Recommendation

**4.10 Treasury Board should ensure that the responsibilities for IT security, as outlined in Treasury Board policy are being complied with.**

### Security Policies and Procedures

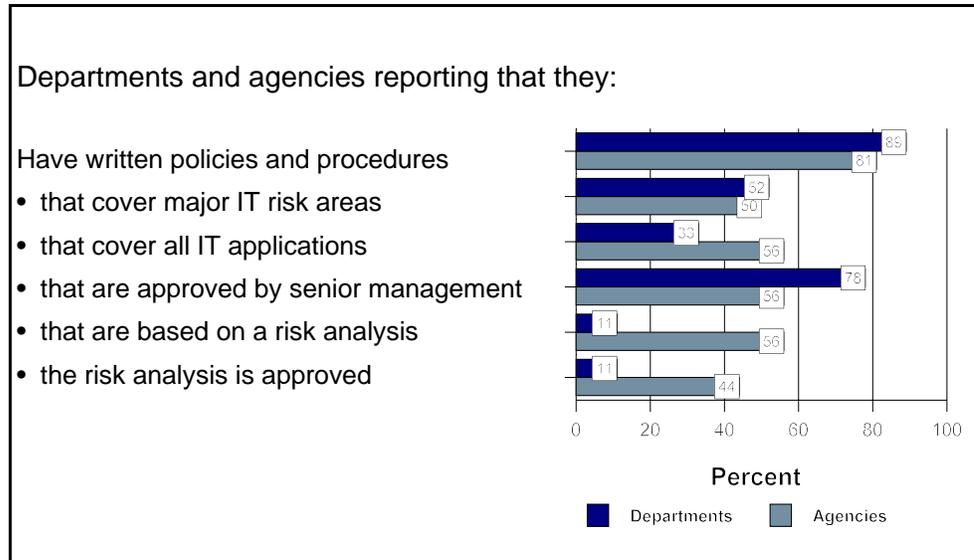
**4.11** IT security policies are important to ensure departments and agencies adequately protect confidential information, and systems are available to process data.

**4.12** Treasury Board has a policy for the secure processing and storage of sensitive government information on information technology delivery systems. The policy applies to departments, and certain crown agencies, and the spirit and intent is expected to apply to all entities. The Treasury Board policy indicates that all sensitive government information and systems are to be protected from unauthorized access, disclosure, removal, modification and interruption.

**4.13** As indicated in **Exhibit 4.2**, most of the departments and agencies surveyed indicated they had overall security policies and procedures which were approved by senior management. They did not usually have policies which were specific to significant applications. We noted that the policies tended to be generic in nature and did not address the specific needs of departments and agencies.

## 4. Information Technology Security Review

### EXHIBIT 4.2 SECURITY POLICY AND PROCEDURES



#### Recommendation

**4.14 Departments and agencies should develop information technology security policies and procedures which address their specific information technology applications.**

#### Information Classification

**4.15** According to Treasury Board policy, information should be categorized for each application in terms of confidentiality, integrity and availability. Confidentiality is the expectation that the information will remain private; integrity is the correctness of the information once it is entered into the computer system; and availability is the maximum acceptable downtime for computer systems before government operations are affected.

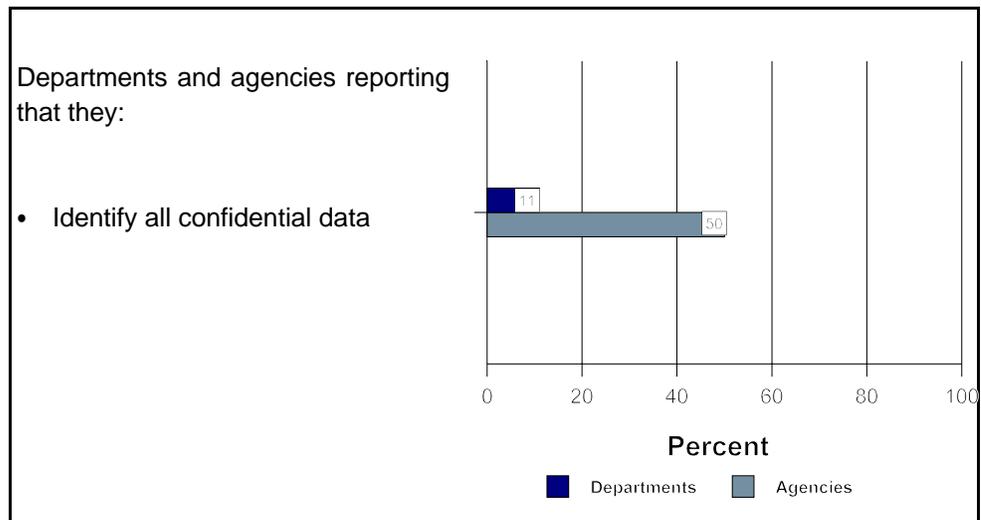
**4.16** Once the information is categorized it should be classified depending on its sensitivity. It is to be classified as public, protected or particularly sensitive. Public information such as legislation is the least sensitive because it is generally available to the public. Protected information would include financial data or health information which

## 4. Information Technology Security Review

would be embarrassing to government or individuals if it were disclosed. Particularly sensitive data would be harmful to individuals, employees or corporations if it were disclosed, and would include information such as: client health records, personnel records or revenue tax records.

**4.17** According to the survey, summarized in **Exhibit 4.3**, only one department and half of the agencies have identified all confidential data maintained on computer systems.

**EXHIBIT 4.3**  
**CONFIDENTIALITY OF DATA**



**4.18** Eight departments and twelve agencies indicate they share confidential information with other government departments and agencies. We noted that there were no documented policies or procedures in place to ensure that the confidentiality and integrity of data is preserved during the process of sharing data with other departments and agencies.

## 4. Information Technology Security Review

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### Recommendations

**4.19 Departments and agencies should follow the information categorization system required in Treasury Board policy.**

**4.20 Policies should be developed to ensure data shared with other departments and agencies is adequately protected.**

### Protection of IT Resources

**4.21** Physical security is important for the protection of IT resources. It includes ensuring local area network servers, communications equipment and personal computers are adequately protected against theft, accidents, floods, fires and other threats. Physical security should also include procedures to control access to computer equipment, as well as infrastructure to protect the equipment. Most departments and agencies had some physical security over computer terminals and servers, and almost every department identified this as an area which needed to be strengthened.

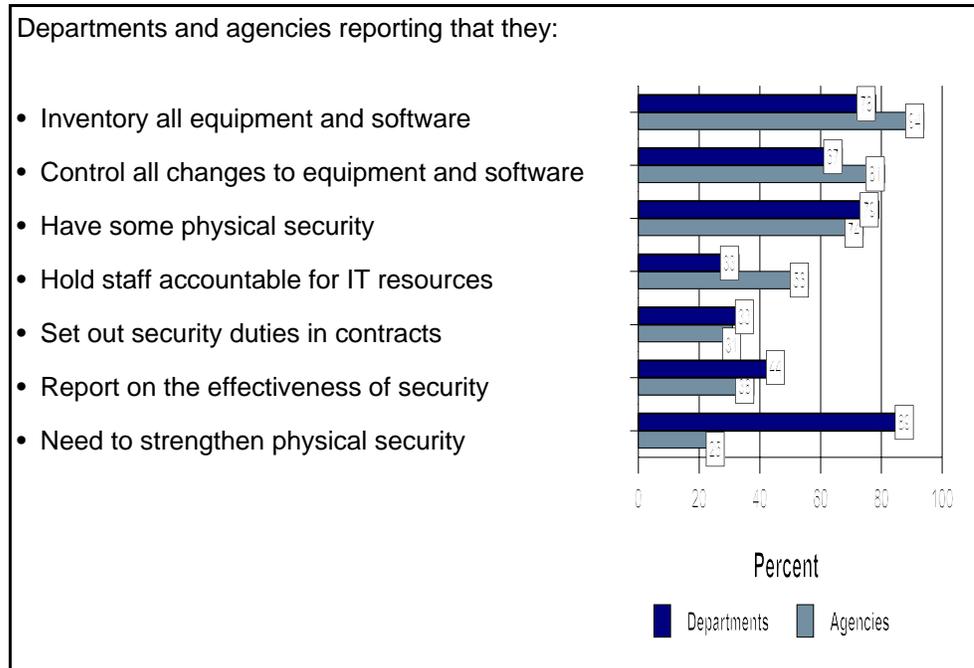
**4.22** Changes to computer hardware and communications equipment should also be adequately controlled. Responsibility for the equipment should be clearly assigned; modifications should be authorized; additions and deletions to the equipment should be reviewed to ensure security is not compromised; and changes should be documented. Most departments and agencies indicated they maintained an up to date inventory of computer hardware and software. Clearly defined processes were usually indicated to be in place to control changes to hardware.

**4.23** Computer programs should be protected to ensure they continue to operate properly. Changes to programs should be approved, documented and performed in a test environment before production programs are affected. Access to programs for production, audit, and changes should be logged. Back-up programs should be securely stored off-site. While most departments and agencies indicated they had a clearly defined process in place to control changes to computer software, only nine agencies and four departments indicated program change controls were adequately

## 4. Information Technology Security Review

addressed by written policies and procedures. A summary of responses related to the protection of computer hardware and software is included in **Exhibit 4.4**.

### EXHIBIT 4.4 PROTECTION OF IT RESOURCES



#### Recommendations

**4.24 The physical security over computer equipment and software should be reviewed to ensure the exposure to damage and loss is minimized.**

**4.25 Policies should be developed to ensure computer program changes are adequately controlled.**

#### External Service Providers

**4.26** External service providers are used by many entities to develop and maintain computer systems. For example, the Department of Health and Social Services has 34 agreements with external service

## 4. Information Technology Security Review

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providers for the provision of a variety of services from help desk support to equipment maintenance. External service providers may have access to sensitive client information therefore security requirements need to be specified in contracts.

**4.27** Contracts with external service providers should specifically include:

- the nature of the information which is accessible;
- limitations on the systems employees can access;
- security requirements for communications equipment;
- responsibility for the protection of data;
- screening requirements for employees;
- training of employees in government security policies; and
- accessibility to procedures for audit purposes.

**4.28** Two departments and four agencies indicated they specified security requirements in contracts with external service providers. Respondents to the survey indicated that background security checks of external service providers were not usually performed.

**4.29** No formal policy or system is in place to monitor the actions of external service providers connected to the government network. As a result, there is a potential risk that service provider staff could have access to sensitive data in the systems they support.

### Recommendations

**4.30** A standard section relating to the security of data should be developed and included in all service level agreements with external service providers.

**4.31** A formal policy should be developed and implemented regarding arrangements with external service providers. At a minimum, the policy should allow for the monitoring of service providers with access to sensitive information and provide for the review of security procedures by government staff.

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## 4. Information Technology Security Review

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**4.32 A process should be implemented to log all traffic between government entities and external service providers. These logs should be reviewed on a periodic basis to ensure access is appropriate.**

### *Information Technology Management Group*

**4.33** The Information Technology Management Group (ITMG) acts as an external service provider for many of the smaller departments and agencies within government. The Division provides IT support services such as the help desk, computer technicians, processing facilities, and network services. This arrangement should be formalized in an appropriately worded service level agreement which clearly articulates the expectations of the ITMG, especially in relation to the safeguarding of sensitive information.

### **Recommendation**

**4.34 The Information Technology Management Group should develop a formal service level agreement to clearly define its role and responsibilities in providing services to departments and agencies.**

### **IT System Availability**

**4.35** Departments and agencies should have back-up and recovery procedures to ensure IT systems and data continue to be available if there is a system failure. The impact of a system failure could be significant depending on the system or systems which fail. Impacts could include, for example: suppliers, employees, doctors, pharmacists and welfare recipients who would not receive payments on time; provincial revenues from taxes and fees which could not be recorded; drug plan recipients who could not get prescriptions filled; and individual health information which could not be accessed.

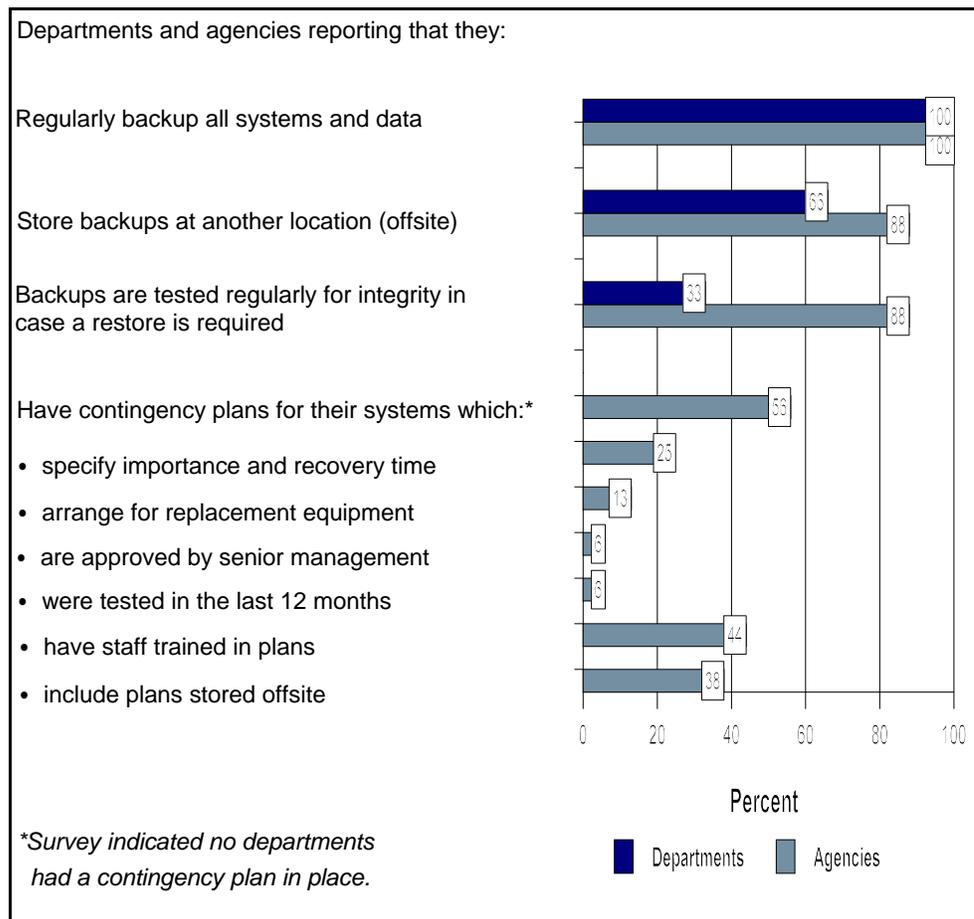
**4.36** Contingency plans (disaster recovery plans) are required to ensure the continued operation of government's IT systems. These plans should be developed, documented and tested to ensure the

## 4. Information Technology Security Review

entity can continue to operate. Part of the planning includes identifying which systems are critical to entity operations.

**4.37** The survey indicated that all departments and agencies regularly backed files up on a timely basis. Most organizations stored back-ups in an appropriate off-site location and some departments and most agencies tested back-ups to ensure they could be used for restorations. The survey indicated that contingency plans were not in place for any departments and approximately half of the agencies. A summary of results is shown as **Exhibit 4.6**.

**EXHIBIT 4.6  
AVAILABILITY OF IT RESOURCES**



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## 4. Information Technology Security Review

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### Recommendation

**4.38** Departments and agencies should ensure that a contingency plan exists for all systems which are critical to their continuous operation. The plan should specify the acceptable recovery time for each system, indicate arrangements for replacement systems, identify a testing plan, indicate staff training requirements and indicate offsite storage for the plan.

### Remote System Access

**4.39** Remote system access allows employees and other users outside the established networks to access government computer systems. This type of access requires different security arrangements because the user must be authenticated and the access must be controlled and logged to ensure it is appropriate.

**4.40** Users access the government network through the ITMG virtual private network (VPN). A virtual private network uses the public wires which connect the internet, to create a network. The system uses encryption to ensure only authorized users can access the network and the data can not be intercepted. We had findings and recommendations related to remote system access which were reported to management. The details are not reported in this report due to the confidential nature of the material.

### Firewalls

**4.41** Firewalls are used to protect the Province's computer networks from unauthorized communications access and attacks from outside the network. A typical firewall would be connected between the government network and the internet to filter all traffic accessing the systems. The system would be used to identify attacks on the system from computer viruses or inappropriate access to sensitive information.

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#### **4. Information Technology Security Review**

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**4.42** We found there were limited policies and procedures in place for management of the firewall. Management of the firewall would include a process to effectively monitor firewall logs to identify and mitigate the risk of a security breach, procedures for the retention of firewall log files which would identify inappropriate activities, and procedures for the modification of firewall rules.

<p><b>Recommendation</b></p>
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<p><b>4.43 Policies and procedures should be developed for the effective management of the firewall.</b></p>
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#### **MANAGEMENT RESPONSE**

**4.44** Our report was discussed with Management and they indicated that the issues raised will be addressed.

## 5. CONSTRUCTION OF THE ATLANTIC TECHNOLOGY CENTRE

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### BACKGROUND

**5.1** In September 2000, Executive Council approved the establishment of the Atlantic Technology Centre (ATC). The ATC was designed to be a state-of-the-art, “smart” facility dedicated to strategic business development within PEI’s emerging information technology industry. The stated objectives were first to create long term sustainable employment and wealth generating capacity for the Province through the support of local technology companies and second, to leverage the Centre as a key business development tool to attract outside interest from leading IT companies.

**5.2** The Centre would be owned and managed through a subsidiary of Technology PEI Inc. and the Province would seek an exit position in year five of operations. The construction costs were to be funded partially from non-repayable sources combined with an affordable mortgage repaid from future revenues.

**5.3** In June of 2000 the Province announced it would be hosting Softworld 2002, an international IT conference which would bring delegates to Prince Edward Island providing a unique opportunity to network, market products and ideas, and attract potential investors to the Province. The conference date of September 2002 became the completion date for construction of the technology centre.

**5.4** The design and fit up of the facility were revised at various points throughout the project with the final costs and funding sources as indicated in **Exhibit 5.1**.

## 5. Construction of the Atlantic Technology Centre

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### EXHIBIT 5.1 PROJECT COSTS AND FUNDING (\$000)

<u>Project Costs</u>		<u>Funding</u>	
Building	\$15,500	Provincial Grants	\$ 4,300
Land and Site Work	2,300	Regional Econ. Dev. Agreement	
Technology and Fit-Up	3,300	(60% Federal - 40% Provincial)	3,200
Design and Professional	1,500	Labour Market Dev. Agreement	1,000
Interactive Theatre	900	IIDI Loan	2,200
Other	<u>200</u>	Mortgage	12,100
		Capital Lease	<u>900</u>
<b>Total</b>	<b><u>\$23,700</u></b>	<b>Total</b>	<b><u>\$23,700</u></b>

**5.5** The Province has accepted essentially the entire risk for this \$23.7 million development project including direct provincial contributions of \$4.3 million; the provincial portion of Federal/Provincial program funding of \$1.3 million; and both the IIDI loan of \$2.2 million and the commercial mortgage of \$12.1 million are provincially guaranteed. Based on information presented to Treasury Board, it is estimated that the Centre will incur operating losses for the foreseeable future.

### OBJECTIVES AND SCOPE

**5.6** In accordance with Section 13 of the Audit Act, we conducted an examination to assess whether appropriate management procedures were in place over the planning, design, construction, and financing of the Atlantic Technology Centre. We expected the needs to be identified and incorporated into the design, funding to be in place prior to construction, appropriate approvals to be obtained throughout the project, project management to be carried out in accordance with best practices, and goods and services to be obtained through a fair and objective process. In addition, we reviewed the leasing of corporate space at the Atlantic Technology Centre in relation to the original projections.

**5.7** During our examination, we reviewed planning and design information and supporting documents, construction and consultants' contracts, financial records, lease agreements, as well as Treasury

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## 5. Construction of the Atlantic Technology Centre

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Board and Executive Council approvals and numerous other documents. In addition, we interviewed staff of ATC Inc. and its parent corporation, Technology PEI Inc.

**5.8** We performed our examination in accordance with the value for money auditing standards of the Canadian Institute of Chartered Accountants, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

### DETAILED AUDIT OBSERVATIONS

#### Accountability

**5.9** In September 2000 Treasury Board approved the establishment of the Atlantic Technology Centre Inc. as a subsidiary corporation to Technology PEI Inc., which itself is a subsidiary of the Crown corporation, PEI Business Development Inc. In February 2001, a submission was made to Treasury Board seeking approval to proceed to construction. In that submission a proposed board of directors was referred to which included representatives from the Provincial government, major funding partners, the industry association, as well as Holland College and UPEI.

**5.10** Typical for a capital project of this size, a number of sources of funding were identified early in the planning stages. We noted that the approval for the Regional Economic Development Agreement (REDA) funding in the amount of \$3.2 million in March 2001 included a condition under section 4.07 of the agreement that UPEI and Holland College be represented on the board of directors of Atlantic Technology Centre Inc. The Atlantic Technology Centre Inc. was incorporated in February 2001 with three directors; the Deputy Minister of Development and Technology, the Chief Executive Officer of Technology PEI Inc., and the Chief Financial Officer of PEI Business Development Inc.

**5.11** Treasury Board's Capital Projects Management Policy was developed to guide the planning for capital projects. The Policy applies to entities on Schedule A and B of the Financial Administration Act. For other government entities the general intent

## 5. Construction of the Atlantic Technology Centre

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of the Policy should be used as a guideline. In this case, a government-owned corporation was established, the Atlantic Technology Centre Inc., to construct and own the centre. The policy requires that procedures be established for authorization and project management. We expected the board of directors of ATC Inc. to provide direction and accountability for the project management team.

**5.12** The planning and design of the Centre was carried out in 2000-01. The construction began in the summer of 2001 and tenants began moving in by October 2002. During the planning and construction period the project management team met frequently and made many design decisions and project alterations. The Project Management Team leader indicated that senior management of the Department of Development and Technology was aware of major decisions made by the team but could not provide documented approval. We noted that the board of directors of ATC Inc. did not meet on a regular basis to provide oversight to the project. The board met for the first time in July 2002 and not again until August 2003.

### **Recommendations**

**5.13 Conditions attached to funding agreements should be complied with.**

**5.14 When major construction projects are undertaken, an appropriate accountability process should be used which defines the authority of the project management team and provides the link to Treasury Board and Executive Council.**

### **Project Management**

**5.15** Management of the design and construction of the ATC project was primarily carried out by two teams. The design team began meeting after the architect was hired in November 2000 and continued meeting until the construction contract was awarded in July 2001. The project team began meeting in February 2001 and continued until January 2003. The project team included the design team members, excluding the architectural firm representative, as well as the CEO of Technology PEI and a number of staff.

## 5. Construction of the Atlantic Technology Centre

**5.16** One of the planning objectives of the Capital Projects Management Policy is to ensure a reasonable assessment of alternatives and options are presented so that Treasury Board and/or Executive Council can make decisions based on complete information. The project cost estimates provided for Treasury Board's approval and the actual costs are summarized in **Exhibit 5.2**.

### EXHIBIT 5.2 COMPARISON OF ESTIMATES AND ACTUAL CAPITAL COSTS (\$ MILLIONS)

	Estimates			Actual
	Sept. 2000	Feb. 2001	Aug. 2002	Oct. 2003
Land	\$ -	\$ 1.0	\$ 1.2	\$ 1.0
Site work	.3	.4	1.3	1.3
Construction - Base Building	13.5	16.4	15.4	15.5
Technology and Fit-up	2.7	1.2	3.1	3.3
Design fees	.7	1.1	1.5	1.5
Interactive Theatre	-	-	.9	.9
Other	.3	.5	.3	.2
Total	<u>\$17.5</u>	<u>\$20.6</u>	<u>\$23.7</u>	<u>\$23.7</u>

**5.17** The August 2002 submission, approved by Treasury Board, provided total project costs at \$22.8 million but also included a lease arrangement used to finance the purchase by ATC Inc. of interactive multi media equipment over a five year period costing \$.9 million. This arrangement has been recorded as a capital lease in the financial statements of ATC Inc.

**5.18** In summary the Treasury Board approvals provided for the following:

- In September 2000, for \$1 million to carry out design and site work;
- In February 2001, for \$20.6 million to complete design and tender the construction contract;
- In July 2001, to award the construction contract, project budget to remain at \$20.6 million; and

## 5. Construction of the Atlantic Technology Centre

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- In August 2002, for an additional \$3.1 million to complete the project, total costs \$23.7 million.

**5.19** We expected submissions to Treasury Board would provide the information necessary to achieve the objectives described in the policy, however, we found the Treasury Board submissions were not always made in a timely manner and in some cases lacked the degree of detail normally provided for major capital projects.

**5.20** In the September 2000 submission to Treasury Board a draft business plan for the ATC was provided as support for the approval. In its decision, Executive Council specifically directed the Minister of Development and Technology to report back to Cabinet when funding partners were confirmed and a comprehensive business plan had been finalized. The plan was important because it would outline the project objectives, capital costs, funding or financing, space utilization, revenues and operating costs. Although certain aspects of the draft business plan were updated and provided as support to subsequent submissions, no updated business plan was completed, as directed by Executive Council.

**5.21** The February 2001 approval by Treasury Board, which was endorsed by Executive Council, gave permission to proceed to construction subject to approval by all funding partners. The project proceeded to a public call for construction tenders in May 2001 without the required confirmation of funding sources being provided to Treasury Board. Funding of \$2 million was expected from the Labour Market Development Agreement (LMDA), however, the agreement signed in April 2001 reduced the LMDA funding for this project to \$1 million with a commitment from LMDA to fund \$1 million in unrelated projects sponsored by Technology PEI and PEI Business Development Inc. Treasury Board was not advised of this significant change until August 2002, when construction was nearing completion.

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## 5. Construction of the Atlantic Technology Centre

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### Recommendations

**5.22 Information requested by Executive Council or Treasury Board should be provided.**

**5.23 Capital projects should not proceed without meeting the conditions of Treasury Board approval.**

### Land Assembly

**5.24** In 1999, Treasury Board approved a commitment of \$1 million toward the purchase of the former Eaton's property by Charlottetown Area Development Corporation (CADC) for \$1.5 million. The City of Charlottetown paid the other \$.5 million which was attributed to the back parking lot portion. In anticipation of a parking garage development, the City acquired a number of other properties in the vicinity of the former Eaton's property for \$800,000.

**5.25** When the preferred location for the ATC was decided, the Province and the City agreed to a land transfer. CADC paid the City \$1.3 million for the land it had acquired, i.e., \$500,000 for the former Eaton's parking lot and \$800,000 for the other properties. Treasury Board directed ATC Inc. to pay \$1 million to CADC as originally agreed for the former Eaton's property. The net effect is that ATC Inc. paid \$1 million for property that cost \$800,000. In addition, the costs of demolition of the former Eaton's building were charged to the ATC project costs in the amount of \$200,000.

### Construction Contract

**5.26** The general construction contract was awarded in July 2001 for \$15.9 million. A twelve month construction schedule was expected, however, the architect's discussions with contractors indicated from the outset that this schedule would be difficult to meet.

**5.27** The facility is constructed on a site that previously held a service station and drycleaner. Consultants were retained to carry out an environmental site assessment and an estimated cost for site

## 5. Construction of the Atlantic Technology Centre

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clean up was established at \$115,000. When excavation began in August 2001 the extent of hydrocarbon contamination was greater than expected and drycleaning solvent was discovered that had not been found during previous investigations. The costs to clean up the site and provide additional protection from future contamination was \$1.1 million. The contaminated soil had been estimated at up to 2,400 tonnes, however, the actual exceeded 38,000 tonnes.

**5.28** Under the contract, construction was to reach substantial performance by August 2002. The architect certified that substantial performance was achieved in September 2002 for architectural and October 2002 for electrical, however, the mechanical work was not approved until February 2003. The general contractor disputed the dates for substantial performance and also disagreed with deficiency holdbacks. The dispute resulted in liens filed against the project by the general contractor and five subcontractors, however, a settlement agreement was reached in October 2003.

**5.29** The settlement agreement included paying the general contractor \$302,000 less \$192,000 in ATC Inc. costs for lost revenue and liquidated damages or a net cost of \$110,000. There were numerous meetings and correspondence with the general contractor by the architect and ATC construction management staff in order to resolve the dispute and have the work completed.

**5.30** The total contract value was revised from the \$15.9 million awarded to \$17.5 million which included \$1.6 million in change orders as summarized in **Exhibit 5.3**. We were unable to locate signed copies of all change orders and were informed they were misplaced. We were advised by construction management staff that all amounts have been agreed to with the general contractor and signed copies were in the process of being obtained, at the time of our audit.

## 5. Construction of the Atlantic Technology Centre

### EXHIBIT 5.3 CONSTRUCTION CONTRACT CHANGE ORDERS

Site remediation	\$1,067,000	
Post production	629,000	
Other, including settlement	<u>114,000</u>	\$1,810,000
Cash allowance, included in contract	\$ (706,000)	
Interior walls	<u>521,000</u>	<u>(185,000)</u>
Total		<u>\$1,625,000</u>

#### Recommendation

**5.31 Signed change orders should be obtained for all changes to construction contracts.**

#### Technology

**5.32** The nature and type of technology that would be available to all tenants of the facility as well as the technology available for content development by multi-media firms were important to the objectives of the project. The project team considered that sophisticated technology would be necessary in order to attract the calibre of tenants envisioned by the project objectives.

**5.33** We noted that the Treasury Board submission of February 2001 included in the project budget \$1.2 million referred to as base technology. In addition the submission referred to a further \$2.9 million in enhanced technology that was not included in the approved project costs. It was anticipated that funding for this enhanced technology infrastructure would be secured through public-private partnerships with technology firms under co-investment agreements. This technology was considered necessary to properly position the Centre with research, development and production capacity but at that time it was unfunded. We found that the actual fit-up and technology costs amounted to \$3.3 million, excluding the cost of the interactive theatre. Fit-up and technology costs include computers, plasma display screens, network equipment, audio visual equipment, boardroom furniture, cabling, and post production fit-up.

## 5. Construction of the Atlantic Technology Centre

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**5.34** Certain technology was added to the facility with the intention that if the technology was available locally it would result in expansion of existing business, new businesses being created that would use the technology or, businesses locating here from off Island. We would expect in any development initiative that a feasibility study would be conducted to determine if the potential market existed for the product or service supported. We noted that an independent consultant was engaged to conduct a study of the interactive multimedia theatre. The study concluded that this type of cinema required high traffic volume in the form of paid admissions to be financially viable. The study also concluded that other revenue sources, such as businesses and research organizations using the technology for development purposes, did not appear to offer a volume and price combination which would justify the capital investment.

**5.35** The interactive theatre was acquired at a cost of \$.9 million in spite of the results of the study. The fit-up costs were added to the capital cost of the project and the equipment was acquired through a capital lease arrangement. We noted that in the Treasury Board submission of August 2002 there is no reference to the consultant's report on the feasibility of the interactive theatre. The submission does not request approval to add the interactive theatre rather it is stated that the theatre area has been upgraded. No evidence of approval beyond the level of the project team was provided to us.

### **Recommendation**

**5.36 Significant additions to capital projects should be approved by Treasury Board.**

### **Co-Investment Process**

**5.37** As previously indicated, an estimated \$2.9 million in enhanced technology was not included in project costs in the submission of February 2001, when Treasury Board gave approval to proceed to construction. Funding for this technology was to be accessed from private sector partners through co-investment. Co-investment is defined in the ATC planning documents as contributions which could take the form of:

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## 5. Construction of the Atlantic Technology Centre

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- reduced cost of supplied technology or services;
- cash sponsorship of specialized areas within the ATC;
- donation of technology, equipment, etc;
- knowledge transfer;
- funding of researcher positions to be located at the ATC.

**5.38** In return, recognition by Technology PEI and the ATC would take the form of but not be limited to:

- preferred supplier status;
- offset against leaseable corporate space;
- assistance with access to local investment opportunities.

**5.39** In June 2001, the project team initiated a request for “Expressions of Interest” (EOI) for firms interested in co-investment in this unique facility. The EOI process has been used in other projects within government. By its nature it is broad and is used where the specifics of the products or services have not been defined. It is essentially inviting companies to come forward and convince the project team that they have the products and services to fill the needs.

**5.40** While there are no regulations or policies over what is an appropriate EOI process, we considered the following to be reasonable business practices:

- advertisement allowing a fair cross section of businesses the opportunity to respond;
- a description of the project requirements and/or needs;
- a time frame;
- an evaluation team;
- an evaluation process including at least a weighting of certain considerations such as price, service, experience, and quality.

**5.41** We were advised that the EOI was advertised on the ATC web site and references were posted on the government web site to the ATC web site for further information and opportunities. In addition direct contact was made with leading innovators in the IT sector.

## 5. Construction of the Atlantic Technology Centre

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**5.42** We were advised that the evaluations were tailored to the circumstances of the EOI respondent. We were provided with an evaluation report prepared by a consultant engaged to carry out the evaluation for the audio visual systems proposals. In the case of the evaluation for the computer hardware, an internal evaluation team was established and prepared an evaluation report on the proposals. In other cases, the evaluation essentially took the form of a negotiation process with the primary respondent.

**5.43** Developing a relationship with a private sector business to partner in acquiring products and services is one aspect of co-investment, establishing a value for the outcome of the relationship is much more difficult. In the Treasury Board submission of August 2002, information was provided to Treasury Board which listed vendors and a coinciding value for co-investment agreements that were indicated as being either concluded or agreed in principle. **Exhibit 5.4** provides this list and compares it to a list of co-investment which was provided to us in August 2003.

### EXHIBIT 5.4 CO-INVESTMENT AGREEMENTS (\$000)

Product/Service Vendor	August 2002	August 2003
Furniture systems	\$ 425	\$ 344
Network system	225	180
Computer hardware	300	108
Carrier infrastructure	250	215
Video system display	130	33
Network services	400	520
Connectivity	20	0
Content development lab	1,000	0
<b>Total</b>	<b>\$2,750</b>	<b>\$1,400</b>

**5.44** We examined the service level agreement signed with the network service provider. The agreement provides management services and access to equipment, which ATC Inc. has valued at

## 5. Construction of the Atlantic Technology Centre

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\$520,000, in exchange for a monthly charge. Although in this case ATC Inc. is not acquiring the equipment directly through a capital investment, it is still paying a substantial fee and there is nothing to indicate that it is receiving any discount or donation. In our view, this arrangement does not meet the definition of co-investment as provided in the ATC's planning documents but is merely a financing arrangement.

**5.45** The Treasury Board submission of August 2002 states in its description that the purchase of an interactive immersion theatre financed by ATC Inc. through a capital lease agreement, will leverage additional investment of \$1 million toward a post production studio. As indicated in the Treasury Board submission, the \$1 million was listed as co-investment from the supplier of the theatre technology. In discussions with the Project Management Team leader, we determined that it was never the intention for the company to provide investment in the capital acquisition of a post production studio. The co-investment of \$1 million was an estimate of financing programs through ACOA and Technology PEI that would be available to prospective clients who would use the post production studio for development initiatives. This is not co-investment in ATC as described in the planning documents.

### **Recommendation**

**5.46 The information provided to Treasury Board on major capital projects should clearly describe all the financial implications of the project.**

### **Revenues**

**5.47** Major capital projects such as the construction of the Atlantic Technology Centre require not only a significant financial commitment during construction but can also have an impact on future budgets. The Capital Projects Management Policy covers the need to identify the estimated impact of the project on the budgets of government. The Atlantic Technology Centre is designed to encourage economic development in the IT sector. To nurture small start up companies and encourage partnerships and innovation, the

## 5. Construction of the Atlantic Technology Centre

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concept was for a diverse group of IT companies to locate within the Centre. This leased corporate space would provide a stable revenue stream to offset ongoing operating costs of the facility. In addition, the Centre would contain training labs, interactive theatre, production and sound studios which would be used to develop multi media content, and would generate revenue as they were used. Several spaces were included in the design which would provide amenities to the tenants such as a café area, and a wellness centre. The intention was for private sector businesses to lease this space and provide these services to the tenants. And finally there are common areas and unusable space which is non-revenue generating.

**5.48** We reviewed the space allocations for the ATC as indicated in the RFP for architectural services, the cash flow projection prepared when Treasury Board approved the project in February 2001 and the actual constructed amounts as provided by staff of ATC. **Exhibit 5.5** summarizes the changes in the space allocations.

### EXHIBIT 5.5 SPACE ALLOCATIONS (SQUARE FEET)

	Sept. 2000	Feb. 2001	Oct. 2003
Corporate Tenants	47,000	77,000	56,000
Training/Labs/Theatre	29,000	24,000	22,000
Café, Commercial	6,000	8,000	8,000
Common areas/ other	28,000	19,000	37,000
Total	110,000	128,000	123,000

**5.49** The corporate space amounts to approximately 45 percent of the total space within the facility. ATC Inc has been successful in attracting tenants and as of October 1, 2003, there were 16 tenants leasing 48,566 square feet of space or 87 percent of the total corporate space.

**5.50** We noted that of these 16 tenants four were receiving a rental subsidy through Technology PEI, the parent of ATC Inc. The rental incentive program allows eligible businesses leasing space in ATC to

## 5. Construction of the Atlantic Technology Centre

receive a subsidy of \$10 per square foot to a maximum of \$50,000 over the first three years of occupancy. For the four recipients the rental incentive amounted to \$91,000.

**5.51** Nearly 20 percent of the total usable space consists of conference rooms, training labs, theatre, and studios which are rented out on a short term basis. The revenue projections presented to Treasury Board estimate a significant income to be received by ATC Inc. for the short term rent of these facilities. **Exhibit 5.6** shows the projected and actual revenue for 2002-03 as well as the budgeted revenue for 2003-04 and actual to September 2003. As illustrated, for 2003-04 the revenues for other space are substantially below projections. There is a revenue item of \$200,000 which is related to an agreement with the network service provider for resale of the network services to tenants within the ATC. Minimal revenue has been generated through this means. Additional funds will be required to cover operating expenditures before the end of the fiscal year if this revenue trend continues.

### EXHIBIT 5.6 PROJECTED AND ACTUAL REVENUES (\$000)

	Projected Revenues 2002-03	Actual Revenues 2002-03	Budgeted Revenues 2003-04	Actual to Sept. 03 6 months
<b>Corporate Space</b>	<b>\$ 601</b>	<b>\$ 289</b>	<b>\$1,271</b>	<b>\$523</b>
<b>Other</b>				
Speciality Areas	321	63	413	38
Commercial	73	-	71	-
Mechanical/Data	20	-	72	-
Services (video,network)	-	3	200	9
	<b>414</b>	<b>66</b>	<b>756</b>	<b>47</b>
<b>Grant: Technology PEI</b>	-	<b>1,074</b>	<b>776</b>	<b>388</b>
<b>Interest</b>	-	<b>19</b>	-	-
<b>Total</b>	<b>\$1,015</b>	<b>\$1,448</b>	<b>\$2,803</b>	<b>\$958</b>

**5.52** The on-going commitment required from government to fund the operations of the ATC changed over the course of design and construction of the Centre. In the Treasury Board submission

## 5. Construction of the Atlantic Technology Centre

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September 2000 there is a projected annual operating shortfall after start up of \$400,000. In the submission to Treasury Board February 2001, the date when approval was received to complete design and tender construction, updated cash flow projections indicated no annual cash funding would be required after year three of operations.

**5.53** A submission was approved in February 2003 for a special warrant to cover operating losses of the Centre for 2002-03 in the amount of \$992,000. In that submission revised operating projections for the Centre again indicated an on-going need for financial support from government to cover operating shortfalls ranging from \$776,000 in 2003-04 to \$61,000 in 2007-08.

### Employment at the ATC

**5.54** One of the objectives of the Atlantic Technology Centre is to create long-term sustainable employment and wealth generating capacity for the Province. The projections at the approval of the project were for 500 persons to be employed at the Centre with an annual payroll of \$20 million, 75 percent of which would be incremental employment. We were advised that no evaluation of employment created has been conducted, however, a tenant survey is planned in the near future. Management advised that within the first 18 month period upon opening, approximately 320 people work at ATC.

#### Recommendation

**5.55** Information should be presented to Executive Council on the results achieved in relation to the objective of employment creation at the ATC.

### MANAGEMENT RESPONSE

**5.56** Our report was recently released to senior management of the Ministry of Development and Technology and a written response was received.

## 6. GOVERNMENT GARAGES

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### BACKGROUND

6.1 The Mechanical Branch of the Highway Maintenance Division services equipment throughout the Province. Total costs in 2002-03 were \$11.7 million, including \$8 million for Government Garage operations. The expenditures for Government Garage operations are summarized in **Exhibit 6.1**, which shows the actual figures for 2001-02 and 2002-03 as well as the budget figures for 2003-04.

#### EXHIBIT 6.1 GOVERNMENT GARAGES EXPENDITURES (MILLIONS)

	<u>2003-04 Budget</u>	<u>2002-03 Actual</u>	<u>2001-02 Actual</u>
Wages/Salaries	\$4.1	\$4.0	\$3.7
Parts	1.8	2.1	1.7
Fuel	.9	1.0	1.0
Administration/Supplies/Travel	<u>.8</u>	<u>.9</u>	<u>.9</u>
	<u>\$7.6</u>	<u>\$8.0</u>	<u>\$7.3</u>

6.2 Government Garages are located in Charlottetown, Bridgetown and Summerside. A breakdown of 2002-03 expenditures by garage is as follows: Charlottetown \$4.5 million; Bridgetown \$1.4 million; and Summerside \$2.1 million. The primary purpose of the garages is to provide repair and maintenance services for the equipment of the Highway Maintenance Division. In addition, they provide service to other Divisions of the Department of Transportation and Public Works as well as service to government owned vehicles in other departments.

### OBJECTIVES AND SCOPE

6.3 In accordance with Section 13 of the Audit Act we conducted an audit of Government Garage operations. Our audit objective was to assess management practices and controls over government

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## 6. Government Garages

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garages. The scope of the audit included expenditures of the three garages for the year ended March 31, 2003.

**6.4** The examination was performed in accordance with the value for money auditing standards of the Canadian Institute of Chartered Accountants and accordingly included such tests and other procedures as we considered necessary in the circumstances. In conducting our work we interviewed staff, reviewed reports, sampled purchases and analyzed financial information.

### DETAILED AUDIT OBSERVATIONS

#### Purchasing

**6.5** At the time of our audit the Regulations to the Public Purchasing Act required goods over \$1,500 to be tendered through Procurement Services unless the goods were only available from a certain manufacturer or supplier, or an emergency purchase was required to protect life or property. In addition, there is an exemption under the Regulations to the Public Purchasing Act for repair parts for road maintenance vehicles and equipment. The majority of parts purchased by the garages fall into these categories and therefore, the amount of tendering is limited.

**6.6** In 2002-03 approximately \$2.5 million in parts and other non fuel supplies were purchased, of which approximately \$500,000 was acquired by tender or some form of competitive process.

**6.7** The ability to plan ahead for parts purchases is sometimes difficult because many repairs require parts to be ordered and delivered as soon as possible to avoid delays in putting the equipment back in service. We noted that most purchase orders are issued after the parts have been received, as confirmation-only purchase orders. This type of purchasing does not ensure parts are acquired economically, and the use of confirmation-only purchase orders should be minimized.

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## 6. Government Garages

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### Recommendation

**6.8 The Government Garages should monitor the use of purchase orders to ensure the use of confirmation-only purchase orders is minimized.**

**6.9** We reviewed a sample of purchases for each garage. Our objective was to assess purchasing practices and test the accuracy of costs recorded. The sample of tendered purchases indicated some weaknesses in the procedures being followed which are described in the following paragraphs.

#### *Tires*

**6.10** The total value of tires purchased in 2002-03 was \$158,000. Tires are tendered annually, however, our sample indicated differences between invoiced prices and tendered prices.

**6.11** For the sample of tire purchases, invoiced prices exceeded the tendered prices by \$9,600 and, in other cases, invoiced prices were lower than tendered prices by \$3,000. In most cases, prices invoiced were not checked against the tendered prices. The tendered prices were not provided to all the garages.

**6.12** A large portion of the \$9,600 difference from tendered prices related to two tire sizes. One tire size was used on heavy trucks, 15 were purchased costing \$640 each although the tendered price was \$445. The other tire size was used on graders, 13 were purchased at \$1,075 each although the tender price was \$727. The truck tires purchased had a higher rating and were a different product code than those included in the tender.

**6.13** The tire purchase estimates provided in the tender appeared high. We reviewed the radial tire section of the 2003-04 tender and estimated tire purchases were twice as high as the actual usage for 2002-03. Tire usage data is maintained which would assist in planning the tire tender, however, inconsistent part code numbering limits the ability to accurately summarize the data.

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## 6. Government Garages

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### Recommendations

**6.14** The Government Garages should compare the invoiced prices for tires against the tendered price.

**6.15** To assist in monitoring tire usage and planning for future requirements, the Government Garages should consider implementing a consistent part numbering and identification system for tires.

### *Fuel*

**6.16** The garages purchased approximately \$1 million of gas and diesel fuel in 2002-03. Fuel is tendered on a government-wide basis and is awarded based on a discount off the maximum price that is approved by the Island Regulatory and Appeals Commission (IRAC).

**6.17** During our audit we noted that Charlottetown purchased unmarked gas, however, Summerside purchased marked gas. Marked gas is purchased tax exempt and its usage is restricted. The Charlottetown Garage was charged \$25,000 in taxes. Although this amount would eventually be remitted by the fuel distributor to Provincial Treasury, it results in increased expenditures for the Department of Transportation and Public Works. Subsequent to our field work, department staff advised that marked gas is now being delivered in Charlottetown.

### *Fuel Usage Monitoring*

**6.18** All vehicles which refuel at the garages are to provide their meter readings at the time. For vehicles which are refuelled in the field, operators are to phone in their meter readings on a weekly basis. We reviewed a sample of fuel records for graders and heavy trucks. We found that the vehicle meter readings entered on the computerized FleetAnywhere System were not accurate. Over 400 entries totalling \$19,000 for 81 different vehicles had a zero meter reading indicated. In addition, many vehicles have the same meter reading for several deliveries. Staff used the date of manual posting of the entry to the system instead of the actual delivery date. The

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## 6. Government Garages

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vehicle meter readings should be properly recorded in order to correctly compile consumption data.

**6.19** Standard reports are not prepared on fuel usage. Regular reports in a standard format such as fuel usage over distance driven would highlight items requiring follow-up. Regular reporting and monitoring of fuel is necessary to ensure usage is controlled and records are accurate.

**6.20** In most cases, gas credit cards are used for vehicles that operate some distance away from the tanks in Charlottetown or Summerside. We found fuel purchases by credit card are not added to the computerized FleetAnywhere data and therefore, any reports produced by the system, on fuel consumption for light vehicles, would be incomplete.

### **Recommendations**

**6.21** The Government Garages should prepare standard fuel usage reports and review for unusual items.

**6.22** The fuel usage recorded in the FleetAnywhere System for light vehicles should include credit card purchases.

### **FleetAnywhere**

**6.23** FleetAnywhere, a fleet management system, was introduced during 2000 to track parts, shop floor activities, and fuel usage for the fleet of government owned and leased vehicles.

**6.24** The Department paid over \$64,000 for the system, however, there are some system capabilities which are not being fully utilized. These include:

- Interface to Oracle Financials for purchasing;
- Download to spreadsheet applications;
- Parts inventory fully integrated with Oracle Financials;
- Fuel consumption reports;

## 6. Government Garages

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- Summary reports of work orders; and
- Vehicle cost reports.

**6.25** Department management indicated that the system is capable of performing these functions, however they are not currently used. We were advised by the Department that the interface to Oracle Financials is not completed because it has not been enabled by the Comptroller's Office.

**6.26** Because the full potential of the system has not been realized, staff at each garage are spending considerable time entering data into the system and a number of useful reports are not being produced for management.

### Recommendations

**6.27** The Department should review the fleet management system and determine why the system capabilities are not being used.

**6.28** The Government Garages should use the FleetAnywhere System to prepare standard management reports on a regular basis for each location.

### *Labour Costs*

**6.29** The FleetAnywhere System records labour hours and labour costs by work order. Employees are required to indicate the hours worked on each assigned work order. When a work order is completed the labour hours for each employee are entered. The system then calculates labour costs based on the hourly rates set up for each employee.

**6.30** Each garage location uses shop work orders to accumulate time which is not charged directly to equipment. The total hours charged to shop work orders in 2002-03 was 9,150. Shop work orders can include time on assigned tasks, such as welding or machining as well as unassigned time such as vacation and sick leave. There is no breakdown of time charged to shop work orders. In our opinion, time

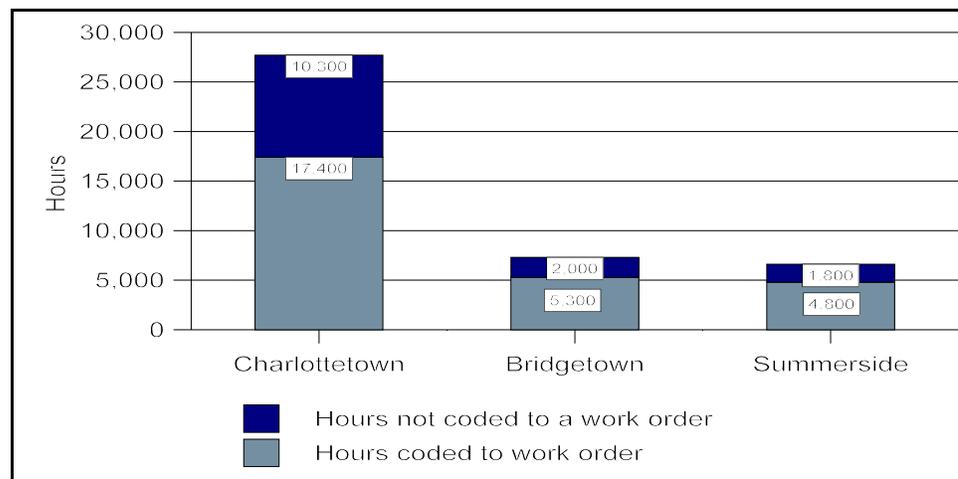
## 6. Government Garages

charged to shop work orders should be more precisely allocated to the projects or tasks assigned.

**6.31** A time card system is used to support the government payroll system. This system records all hours paid including vacation and sick time but does not accumulate any work order data.

**6.32** We compared the number of hours paid for 2002-03 to those charged to work orders for a sample of employees. As illustrated in **Exhibit 6.2**, for the sample selected, we found that approximately one third of the hours paid were not charged to work orders.

**EXHIBIT 6.2**  
**EMPLOYEE HOURS PAID COMPARED TO**  
**HOURS CHARGED TO WORK ORDERS**  
**SAMPLE RESULTS**



**6.33** A system should be in put in place to account for employee time, including time charged to work orders, as well as unassigned time such as vacation and sick leave.

## 6. Government Garages

### Recommendations

**6.34** The time spent doing work on assigned tasks should be separately identified from other time charged to shop work orders.

**6.35** The Government Garages should reconcile the hours of work paid against time entered to FleetAnywhere.

### Staffing

**6.36** Exhibit 6.3 is a summary of the direct labour staff at each of the three garages.

#### EXHIBIT 6.4 DIRECT LABOUR (NUMBER OF EMPLOYEES)

	<u>Mechanics</u>	<u>Welding</u>	<u>Machine Shop</u>	<u>Body Shop</u>	<u>Total</u>
Charlottetown - full-time	22	5	2	3	32
- part-time	4	1	-	4	9
Summerside - full-time	7	4	-	-	11
- part-time	-	-	-	-	-
Bridgetown - full-time	5	2	-	-	7
- part-time	<u>4</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>4</u>
	<u>42</u>	<u>12</u>	<u>2</u>	<u>7</u>	<u>63</u>

**6.37** The Quality Management Plan - Mechanical Branch was developed and approved by senior management in the early 1990s. It was intended to be updated annually although the most recent copy is dated February 1998. The plan indicates that the number of mechanics should be based on the quantity and type of assets serviced. In the plan a mechanic is expected to service 18 light truck vehicles or 12 heavy trucks or 6 pieces of heavy equipment or 72 attachments. The plan indicates the mechanic staffing calculation will be performed every three years, however, management was unable to provide any recent calculation to support the current staffing complement.

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## 6. Government Garages

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**6.38** We applied the staffing calculation to each location and found Summerside and Bridgetown to be in line with the staffing formula. Based on the formula, the Charlottetown garage had more than the required number of staff. The reasons provided were that some equipment worked on is from other regions, and there were significant repair hours charged to older equipment. We did note in our 2002 audit of Highway Maintenance that a number of heavy equipment pieces were past their useful life.

**Recommendation**

**6.39** The Government Garages should update their mechanic staffing formula. It should consider facility and equipment limitations and, the allocation of work to other garage locations.

### MANAGEMENT RESPONSE

**6.40** We have discussed our report with management and they indicated the issues raised will be addressed.

## **7. WATER MANAGEMENT DIVISION**

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### **BACKGROUND**

**7.1** Water Management is a Division of the Department of Environment and Energy. The mandate for the Division is established under the Environmental Protection Act. The Division includes the Drinking Water Management Section, the PEI Analytical Laboratories Section and the Watershed Management Section.

**7.2** The Water Management Division is responsible for the sustainable management, protection and enhancement of the Province's drinking water, groundwater, inland surface water and coastal estuaries. The Division provides water testing services and engineering advisory services to the general public, other provincial departments and agencies, industry and municipalities. In addition, the Division monitors and conducts assessments of the Province's water resources. The Division also regulates water and sewer infrastructure and assists in the administration of funding that supports this infrastructure.

**7.3** Expenditures of the Division are expected to increase significantly from \$1.8 million in 2002-03 to \$2.5 million in 2003-04. The reorganization of the watershed management program accounts for a large portion of this increase. The Division is also responsible for collecting revenue. Total revenues were \$507,000 in 2002-03 and are budgeted at \$424,700 in 2003-04.

### **OBJECTIVE AND SCOPE**

**7.4** In accordance with Section 13 of the Audit Act, we conducted an examination of the Water Management Division of the Department of Environment and Energy. Our objective was to assess the management practices used by the Division.

**7.5** Our examination was performed in accordance with the value for money auditing standards of the Canadian Institute of Chartered Accountants and accordingly included such tests and other procedures as we considered necessary in the circumstances. In

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## 7. Water Management Division

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conducting our work we interviewed staff throughout the Division and examined various reports, documents and files.

### DETAILED AUDIT OBSERVATIONS

#### Planning

**7.6** To ensure the water resources goals of the Department are achieved, the Division should have a well defined planning process. This would normally include: a strategic plan with goals and results to be achieved over the next three to five years; an operational plan which indicates what will be done in the next year; a budget which allocates resources to the operational plan; and a framework to measure performance in relation to goals and expected results.

**7.7** In November 1999, the previous Department of Technology and Environment prepared an Environment Strategic Plan for the period 2000-2005. The strategic plan was for the environmental portion of the mandate of the Department. It included a corporate plan for the Department as well as strategic plans for each Division. According to management this plan continues to be used by the Water Management Division.

**7.8** The Environment Strategic Plan indicates that the goals of the Division are:

- to enhance the quality and sustainability of the Province's groundwater and aquatic ecosystems;
- to increase public acceptance of responsibility for the protection and sustainable use of the water resources;
- to increase public confidence in the programs, services, advice and assistance provided by the Division;
- to increase public knowledge and understanding of groundwater and surface water systems; and
- to improve staff morale and job satisfaction.

The strategic plan identifies strategies to address most of these goals and Division staff have developed a work plan for their implementation.

## **7. Water Management Division**

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**7.9** During the year the Department was reorganized, and watershed management responsibilities were moved to the Water Management Division. The Environment Strategic Plan was not updated to recognize these changes.

**7.10** The Environment Strategic Plan indicates the Department will develop indicators of success for water quality which will be monitored and reported. In addition, the Division will conduct public opinion and client satisfaction surveys to determine if public expectations are being met.

**7.11** During 2003 the Department of Fisheries, Aquaculture and Environment issued a State of the Environment report. As it relates to water, the report indicates the drinking water supply is generally good although nitrate levels in drinking water and surface water are increasing. It also provides indicators related to E.coli in private wells, water and wastewater central servicing and shellfish closures. While this information is useful for Departmental reporting, further information is required to determine whether the goals of the Division are being achieved.

### **Recommendations**

**7.12 The Strategic Plan should be updated and approved by the Department of Environment and Energy.**

**7.13 Indicators should be developed for each of the Division's goals so that results achieved can be measured and reported.**

### **Drinking Water Management Section**

**7.14** The principal responsibility of this Section is to ensure sustainable management, protection and enhancement of drinking water.

**7.15** Prince Edward Island is totally dependent on groundwater for drinking water. Drinking water is provided to approximately 43 percent of households by centralized systems and the remaining 57 percent by private wells.

## 7. Water Management Division

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**7.16** The Department announced a drinking water strategy in June 2001 which includes '10 points to purity'. Following are the points which were still being addressed at the time of our audit and the status of implementation of each:

- To develop water monitoring and public reporting regulations for central water supply and wastewater treatment systems, updating guidelines established in 1999.

*These have been drafted and the intention is to incorporate these changes into broad regulations covering the operation of municipal water and wastewater systems. At the time of our audit these were not approved.*

- To develop Standards and Guidelines for the supply, storage, distribution and maintenance of water systems.

*This document is being developed by the four Atlantic Provinces with projected completion in early 2004.*

- To enforce mandatory certification for water supply and wastewater operators upgrading from the current voluntary certification.

*Certification of water supply and wastewater operators will become mandatory under the broad regulations being developed.*

- To work with municipalities and land owners in the development of a strategy for municipal wellfield protection.

*A hydrogeologist has been hired and protection zones for municipal utilities are being developed. The expected completion date of the strategy is the spring of 2004.*

### *Public Water Suppliers*

**7.17** Public water suppliers are defined as those systems that supply five or more households. Public water suppliers can range from municipal systems servicing 30,000 people to a well serving five

## 7. Water Management Division

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cottages. There is no process in place to identify all public water suppliers. Therefore, there is no way of knowing whether all water supplied to the public is tested on a regular basis. To ensure the public is adequately protected, all water suppliers should be identified, have monitoring programs in place and have strategies to protect their wellfields.

### Recommendations

**7.18 Regulations should be in place to ensure municipal water supply and wastewater treatment systems are monitored and the results reported.**

**7.19 Mandatory certification of all water supply and waste water system operators should be required.**

**7.20 Wellfield protection plans should be completed for municipal wells.**

**7.21 There should be a process in place to ensure all public water suppliers are identified.**

### *Drinking Water Testing*

**7.22** Water quality is determined by comparing the test results with the Guidelines for Canadian Drinking Water Quality prepared by the Federal-Provincial-Territorial Committee on Drinking Water and published by Health Canada.

**7.23** The PEI Analytical Laboratories Section operates microbiology and chemistry laboratories to analyse water samples. The Section uses a computer system to facilitate the notification of clients if water problems need to be addressed, in particular, high coliform and E.coli results identified by the microbiology lab.

**7.24** The Department considers that water samples containing coliform counts less than 10 organisms per 100 ml indicate the water is fit to drink. Coliform counts in samples are an indicator of the

## 7. Water Management Division

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vulnerability of a water supply to contamination. If coliform bacteria are present, it may be possible for E.coli or other harmful bacteria to enter the system. The presence of any E.coli in a water sample indicates the well has been contaminated by sewage or manure and is unsafe to drink.

**7.25** Division procedure for bad water results related to coliform and E.coli is to telephone clients and if contact is made, it is indicated in the computer system that the client has been notified. If contact is not made within three days, the report that is sent by mail to all clients is relied upon as the contact.

**7.26** Additional procedures are to be followed when E.coli is detected in a water sample. The homeowner is to be immediately notified and advised to boil their water, and adjacent homes in the immediately affected area are to be sampled. In addition, staff are to advise residents within 500 feet of the contaminated well and suggest that they have their water tested.

**7.27** We examined the procedures used to track a water sample from receipt through the lab to communication of bad water results. For the sample we examined, staff attempted to contact clients by phone and in the cases where telephone contact was not made within three days, staff relied on the client receiving the test report that is mailed to all clients. In cases where bad water was detected in the water samples, there was insufficient documentation on file to demonstrate that the required procedures were followed. We expected that complete documentation would be maintained on file to indicate the nature, times and dates of contact with homeowners as well as a copy of the correspondence sent to the client.

**7.28** Overall, the incidence of coliform above 10/100 mls in wells sampled has increased significantly in recent years from 8.4 percent in 2001 to 15.8 percent in 2002. The incidence of E.coli has increased from 2.5 percent to 3.7 percent of wells tested. Subsequent to our audit work, we were advised that for 2003 the incidence of coliform over 10/100 mls in wells sampled was 15.8 percent and the incidence of E.coli in wells tested was 2.5 percent.

## 7. Water Management Division

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### Recommendation

**7.29** To demonstrate that the Department has taken action to notify clients of bad water results, the Department should maintain documentation of telephone contacts, correspondence with the client and follow-up action including notification of adjacent homeowners.

### Watershed Management Section

**7.30** The Watershed Management Section is responsible for the management of groundwater, inland surface waters and coastal estuaries. A watershed is all of the land draining its rain, snowmelt and groundwater into a stream or river.

**7.31** A recent reorganization transferred the Wildlife Habitat Improvement Program to the Section and changed the Watershed Coordinators from seasonal to full-time positions.

**7.32** The Section has held strategic planning sessions to establish direction on their broader role in watershed management. Strategies that are being discussed expand on the previous strategic plan and include encouraging community groups to become more involved, continuing to target watersheds where there is community interest and establishing demonstration watersheds. These strategies were not finalized or approved at the time of our audit.

**7.33** In order to manage watersheds more effectively it would be useful for the Section to establish a watershed management strategy.

### Recommendation

**7.34** A watershed management strategy should be completed which includes an assessment for each watershed and a plan to ensure the watersheds are protected.

## 7. Water Management Division

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### *Water Quantity Monitoring*

**7.35** Monitoring water quantity is important to ensure both adequate ground water reserves and stream flow. The Department has 12 observation wells across the Province that automatically monitor water levels daily. The results are made available to the public through the Department's web site. We noted that the posted results on the web site were out of date and contained some data on water levels that was incomplete.

**7.36** All high capacity wells (greater than 50 gallons per minute) and wells to be used for a central water supply system require a Groundwater Exploration Permit. Test information is collected to determine whether the groundwater extraction will have any significant effects on other groundwater users or the environment. In 2002, the Province announced that it would not issue new groundwater irrigation permits until further study of the impacts is complete.

### *Monitoring Ground and Surface Water Quality*

**7.37** Ground and surface water quality has an important impact on drinking water, aquatic habitat, the fishery and recreation.

**7.38** The Federal/Provincial Water Agreement covers monitoring of a number of sites dating back, in some cases, over 30 years. The results were reported in the Water Quality Interpretive Report 1999 which followed up on a report produced in 1978. In general, surface and groundwater quality was reported to be excellent but key areas of concern in the report were soil erosion, nitrate levels, bacterial contamination of shellfish harvesting areas and the occurrence of pesticide residues. Given the importance of the resource, reporting should be more frequent than every 20 years.

**7.39** The State of the Environment report, 2003, provides two indicators for surface water; nitrate concentration in surface water, and shellfish closures. The report indicates that nitrate concentration has more than doubled in the past 20 years. From 1995 to 2000, the

## 7. Water Management Division

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percentage of area closed to shellfish harvest remained relatively constant.

**7.40** The Department is involved in monitoring water quality, however, the State of the Environment Report only reports on two indicators for surface water and three for drinking water and the Water Quality Interpretive Report, which is more comprehensive, is not issued frequently enough.

### Recommendation

**7.41 The Division should report on water quality and quantity on a more frequent basis.**

### PEI Analytical Laboratories Section

**7.42** The PEI Analytical Laboratories Section is responsible for the management of the Province's water microbiological and water chemistry laboratories.

**7.43** During 2003, the Laboratories were accredited by the Standards Council of Canada. This provides formal recognition that the laboratories are competent to perform specific tests. Accreditation is only given to those laboratories that demonstrate competence in their field and conform to international standards. To gain accreditation laboratories must undergo a full technical assessment and maintain that accreditation by having proficiency tests and a complete technical assessment every two years.

### Revenue

**7.44** During 2002-03, the Water Management Division generated approximately \$500,000 in revenue. Almost 70 percent of revenue was for water testing with smaller amounts for monitoring shellfish water quality, water utilities and other programs.

**7.45** The Division does not have a documented policy which provides a rationale for the fees charged for water testing. Fees for water testing are \$12 for microbiology, \$25 for chemistry, \$100 for

## 7. Water Management Division

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water quality certification plus specific fees for various other tests. The client is not subject to further charges if retesting is necessary.

**7.46** In 2002, the laboratories tested 9,523 private wells for microbiology and 3,111 for chemistry. Revenues for the labs for 2002-2003 were \$344,300 compared to direct expenditures of \$601,600.

**7.47** One area of concern was the lack of follow-up on delinquent accounts. The client receives a first invoice, a second invoice and then a delinquent invoice if they leave their account unpaid. No further action is taken except that the client cannot receive further services. As of August 2003, the delinquent list exceeded \$15,000.

**7.48** Water management operates three water utilities in the province with total revenues of \$55,000 in 2002-03. The utility in Georgetown is regulated by the Island Regulatory and Appeals Commission which last set the rates in 1997. The Northport system services six houses and two fish plants and is billed based on rates established by the Department. According to staff, the plan is to request regulated rates. The Alberton system was established in December 2002 and serves four customers. As of August 2003, no rate has been set or bills issued.

### Recommendations

**7.49** The Division should establish a policy for setting laboratory testing fees.

**7.50** Procedures for reviewing and collecting delinquent accounts should be established and followed.

**7.51** Water utility rates for Georgetown, Northport and Alberton should be regulated, updated on a regular basis and customers should be billed accordingly.

### MANAGEMENT RESPONSE

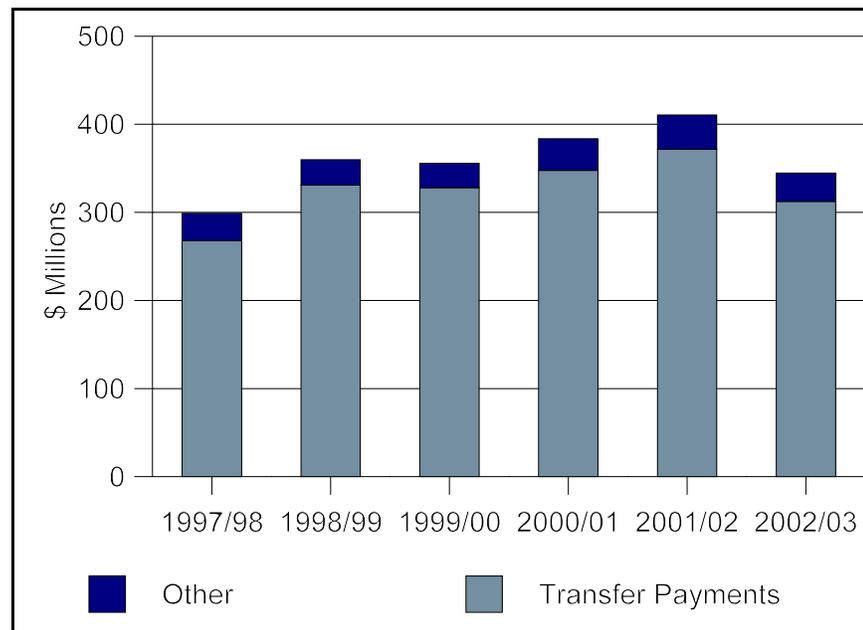
**7.52** Our report was discussed with management and they indicated the issues raised will be addressed.

## 8. FEDERAL CLAIMS

### BACKGROUND

**8.1** Revenues from the federal government provide approximately 35 percent of the total revenues of the Province and in 2002-03 totalled \$345 million. Of this amount, \$1.4 million is capital revenue. Federal revenues dropped in 2002-03 after an increasing trend since 1997-98 as illustrated in **Exhibit 8.1**. The decrease was due primarily to a reduction in transfer payments resulting from revisions to the Province's population as a result of the 2001 census.

**EXHIBIT 8.1  
FEDERAL REVENUES**

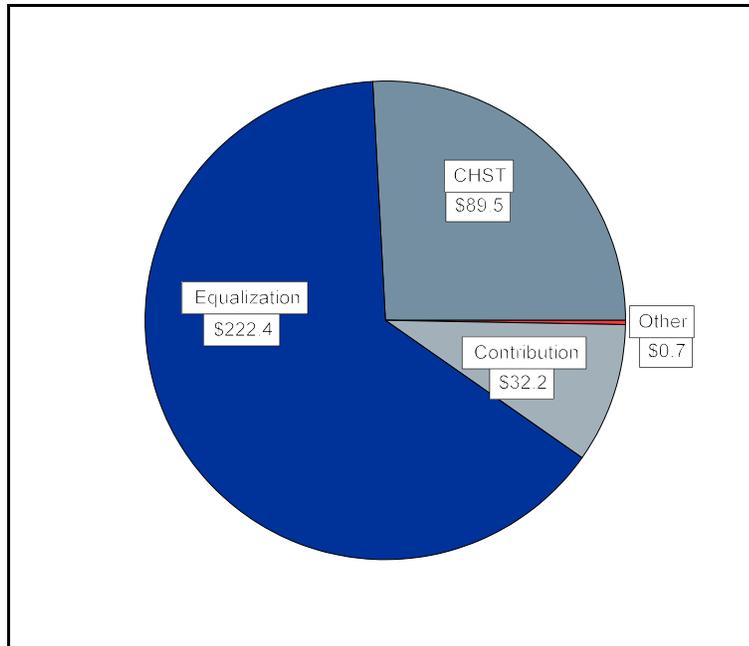


**8.2** Federal revenue is categorized into transfer payments, contribution agreements and other agreements. Federal transfer payments refer to direct transfers which are made by formula to all or most provinces and territories. They are not associated with specific spending by the Province. Contribution agreements support program or project costs funded by the Province. **Exhibit 8.2** summarizes the major federal revenue sources in 2002-03.

## 8. Federal Claims

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### EXHIBIT 8.2 FEDERAL REVENUES 2002-03 (MILLIONS)



**8.3** Equalization is the largest transfer at \$222.4 million and makes up approximately 65 percent of federal revenues. Equalization payments are covered by Part II of the Federal/Provincial Fiscal Arrangements Act and are determined by a defined formula. Payments are received every two weeks by electronic transfer.

**8.4** The Canada Health and Social Transfer (CHST) provides support for health care, post-secondary education and social services. The payment to Prince Edward Island of \$89.5 million equals approximately 26 percent of federal revenues. Part V of the Federal/Provincial Fiscal Arrangements Act covers the CHST which is also received by electronic transfer every two weeks.

**8.5** Revenue from contribution agreements totalled \$32.2 million in 2002-03. The majority of this revenue, \$27.7 million, comes from ten programs.

## 8. Federal Claims

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### OBJECTIVE AND SCOPE

**8.6** In accordance with Section 13 of the Audit Act, we conducted an examination of Federal Claims. Our objective was to assess the management practices related to the preparation, monitoring and accounting for Federal Claims. Our audit included federal/provincial contribution agreements and did not include payments received related to Equalization and the Canada Health and Social Transfer (CHST).

**8.7** We examined all agreements with claims over \$0.5 million in 2002-03 as well as a sample of the smaller claims. Our examination included a review of agreements, communication with the staff responsible for claims processing, and an analysis of claims and supporting financial information.

### DETAILED AUDIT OBSERVATIONS

#### Contribution Agreements

**8.8** Contribution agreements provided \$32.2 million in revenue in 2002-03. These agreements are negotiated with the federal government and allow the Province to recover a portion of the costs of programs. The ten largest agreements are listed in **Exhibit 8.3**. Some of these agreements provide a fixed contribution while others provide cost sharing on a percentage basis.

## 8. Federal Claims

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### EXHIBIT 8.3 CONTRIBUTION AGREEMENTS FEDERAL REVENUE (MILLIONS)

	<u>2002-03</u>
Skills Development Contribution Agreement	\$ 6.4
Agricultural Insurance	6.3
Youth Justice Services	2.4
Infrastructure Program	2.2
Minority and Second Language Education	2.2
Housing Programs	2.0
Primary Care Development	1.9
Promotion of Official Languages	1.5
Canada Health Infostructure Partnership	1.4
Strategic Highway Infrastructure (Capital)	1.4
Other	<u>4.5</u>
	<u>\$32.2</u>

#### Claims Processing

**8.9** Most federal/provincial agreements require that claims be prepared, audited and submitted to the federal government to receive payment. Many agreements also provide for advance payments to be supported by a final annual claim.

**8.10** When we last reviewed Federal Claims in 1992, the Claims Section of the Department of Finance was involved in the preparation and audit of claims. The objective of the Claims Section was to ensure that every shareable expenditure was claimed on a timely basis. While the Claims Section was responsible for most claims, some remained with the various departments.

**8.11** At the time of our audit, all claims were prepared by the department responsible and a few were audited by the Office of the Comptroller. The audited claims include the Infrastructure Program, Promotion of Official Languages and a few small programs depending on the agreements in place each year. There was no centralized monitoring by the Office of the Comptroller except to the extent that

## 8. Federal Claims

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the amount of revenue receivable at year-end is obtained for the preparation of the Public Accounts.

**8.12** As we have reported in the past, there are no policies or guidelines for use by departments in preparing federal claims. Many of the agreements outline a claiming process but it is not always followed. In our view, there should be clear direction on claims preparation, monitoring and follow-up of outstanding claims.

### Recommendation

**8.13 Provincial Treasury should provide direction to departments regarding their role and responsibility related to the preparation, monitoring and accounting for federal/provincial claims.**

### Cash Flow and Interest Costs

**8.14** The timing of cash receipts from the federal government affects the amount of money the Province needs to borrow in the short-term and therefore impacts interest costs. We reviewed the major agreements that provided for advances or interim payments. The most common provisions allow for quarterly advances but terms vary from monthly to an advance at the beginning of the year.

**8.15** We found many agreements that allowed for advances or payments on a certain basis that were not being followed by the departments. To evaluate the impact of the delay in receipts, we compared actual receipts to potential receipts for the most recent three fiscal years. In total, the delay in claiming was estimated to cost the Province approximately \$700,000 in interest charges from April 1, 2000 to December 31, 2003 for claims related to the three previous fiscal years.

**8.16** The Agreement on Minority and Second Language Education provides for three advances and a final claim each year for the main agreement and an advance at the start of the year and final claims for supplementary agreements. The Department typically makes one claim which has been getting later each year and was not complete

## 8. Federal Claims

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as of December 31, 2003 for the March 31, 2003 year end. We estimate that the cost to the Province in interest charges from April 1, 2000 to December 31, 2003 was approximately \$365,000. A significant portion of this results from the supplementary agreement on the Summerside French School. Advances and claims recoverable as far back as June 2000 were not received until April 2003.

**8.17** Under the Youth Justice Agreement, Section 23.(1) provides for Canada to make quarterly payments during the year. The Department historically makes one claim late in the following year. As of December 31, 2003, the March 31, 2003 claim had not been finalized. We estimate that for the past three fiscal years the delayed receipts cost the Province over \$235,000 in interest from April 1, 2000 to December 31, 2003. For the year ended March 31, 2002, payment was not received until March 2003.

**8.18** The Promotion of Official Languages Agreement allows for an initial and a final payment but has historically been claimed after the year end. As of December 31, 2003, final claims had been prepared for 2001-02 and 2002-03 but had not been submitted. Interest costs were estimated at approximately \$125,000 from April 1, 2000 to December 31, 2003.

**8.19** The other agreements we reviewed also had claims that were late but the impact was not significant in relation to those discussed in the previous paragraphs. In our view, administration of federal claims should be improved to ensure claims are submitted on a timely basis.

### Recommendation

**8.20 All claims under federal/provincial contribution agreements should be submitted and collected on a timely basis.**

### MANAGEMENT RESPONSE

**8.21** We discussed our report with management and they indicated the issues raised will be addressed.

# **FINANCIAL STATEMENT AUDITS**



# 9. INTRODUCTION TO FINANCIAL STATEMENT AUDITS

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## INTRODUCTION

**9.1** Section 13 of the Audit Act establishes the Auditor General's mandate to perform financial audits of the Public Accounts, Crown controlled or owned corporations, and the trusts and funds held by any agency of government insofar as they are not subject to financial audit by an external auditor.

**9.2** Financial statements are management's responsibility and reflect management's assertions. They provide information that is used to make important economic decisions. It is imperative that the reader has confidence in the quality of that information.

**9.3** The auditor is independent of management and can objectively assess the accounting principles used and the estimates and other decisions made by management as reflected in the financial statements. An examination of the entity's accounts is carried out in accordance with generally accepted auditing standards. These standards have been established over time and continue to evolve with the changing economic environment. The result of the examination is the auditor's opinion as issued in the Auditor's Report.

**9.4** In addition to issuing an Auditor's Report on the financial statements, the auditor may also identify problems in the financial controls and accounting records. In these cases, findings and recommendations are reported in a management letter addressed to the department or agency.

**9.5** For the majority of the financial statement audits we performed, management letters were issued. We brought to management's attention any problems noted during the audits and made recommendations for improvements. These recommendations are at various stages of implementation.

**9.6** In the following sections we provide summary information on our audits of the Public Accounts and Appropriations.

# 10. PUBLIC ACCOUNTS

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## BACKGROUND

**10.1** The Public Accounts include the annual financial statements of government and are the primary source of information on government's stewardship of public funds both to Islanders and to the Legislative Assembly.

**10.2** The Public Accounts are prepared by the Comptroller and tabled by the Provincial Treasurer in the Legislature as required by the Financial Administration Act. According to the Act, the Public Accounts must contain the Financial Statements of the Operating Fund and the Consolidated Financial Statements of the Province, along with any other statement required by Act to be presented. The Consolidated Financial Statements provide the most complete information about the operating results and financial position of the Province as they consolidate the accounts of the Operating Fund with those of the Crown corporations and agencies.

**10.3** The Public Accounts for the year ended March 31, 2003 consist of two volumes:

- Volume I contains the Consolidated and the Operating Fund audited financial statements.
- Volume II contains the audited financial statements of the Crown corporations and agencies.

## OBJECTIVES AND SCOPE

**10.4** In accordance with the Audit Act, we performed an audit of the Public Accounts of the Province for the year ended March 31, 2003. The objective of our audit was to express an opinion on the financial position and operating results of the Government. Our audit reports on the Consolidated Financial Statements and the Operating Fund Financial Statements for the year ended March 31, 2003 did not contain any qualifications or reservations.

## 10. Public Accounts

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**10.5** Under Section 17 of the Audit Act, the Auditor General is not required to audit or report on the accounts of any agency of government where another auditor has been designated to audit its accounts. In these instances, the Auditor General relies on the Auditor's Report for each of these entities when performing the audit of the Public Accounts.

**10.6** This report contains comments and observations arising from our audit of the Public Accounts for the fiscal year ended March 31, 2003.

### FINANCIAL HIGHLIGHTS

**10.7** Following is a comparison of revenue and expenditure for the past five years from the Consolidated Financial Statements.

	Year Ended March 31				
	(Millions)				
	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>
Provincial Revenue	\$ 632.2	\$ 593.6	\$578.7	\$566.2	\$515.0
Federal Revenue	<u>344.8</u>	<u>410.4</u>	<u>383.7</u>	<u>355.6</u>	<u>359.7</u>
	977.0	1,004.0	962.4	921.8	874.7
Expenditures	<u>1,060.8</u>	<u>1,041.3</u>	<u>997.3</u>	<u>909.4</u>	<u>846.6</u>
Surplus (Deficit)	<u>\$ (83.8)</u>	<u>\$ (37.3)</u>	<u>\$ (34.9)</u>	<u>\$ 12.4</u>	<u>\$ 28.1</u>

### DETAILED AUDIT OBSERVATIONS

#### Financial Statement Presentation

**10.8** For the year ended March 31, 2003 the Consolidated Financial Statements reported a deficit of \$83.8 million compared to a \$65.1 million deficit reported by the Operating Fund. The Operating Fund results are generally significantly different from those contained in the Consolidated Financial Statements. Of the \$18.7 million difference in 2002-03, \$12.9 million pertains to the operating results of the PEI Special Projects Fund and the remaining \$5.8 million relates to the operating results of Crown corporations and agencies within the

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## 10. Public Accounts

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reporting entity which are included in the calculation of the consolidated surplus or deficit.

**10.9** Following is a breakdown of the major components of the surplus (deficit) as recorded on the Consolidated Financial Statements for the past five years.

### CONSOLIDATED SURPLUS (DEFICIT) (Millions)

	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>
Operating Fund	\$(65.1)	\$(17.0)	\$(11.6)	\$(5.4)	\$ 6.3
Special Projects Fund	(12.9)	(7.3)	(17.4)	17.4	23.5
Agencies, Boards and Crown Corporations	<u>(5.8)</u>	<u>(13.0)</u>	<u>(5.9)</u>	<u>.4</u>	<u>(1.7)</u>
Consolidated Surplus (Deficit)	<u>\$(83.8)</u>	<u>\$(37.3)</u>	<u>\$(34.9)</u>	<u>\$12.4</u>	<u>\$28.1</u>

**10.10** Deficits of Crown agencies decreased in 2003 from 2002 largely due to decreased acquisitions of capital assets. The consolidation process requires that accounting policies of Crown agencies be adjusted to conform to the policies of government. Since the Province records the full cost of capital assets as an expenditure in the year of purchase, adjustments are required to the operating results of those agencies which are capitalizing assets.

**10.11** The Consolidated Financial Statements provide a complete picture of Government operations by including the activities of Crown corporations and government agencies. Volume I of the Public Accounts contains the audited financial statements of the Operating Fund and the Consolidated Financial Statements. To avoid confusion and to ensure the Consolidated Financial Statements receive their proper attention, Volume I of the Public Accounts should only contain the Consolidated Financial Statements.

## 10. Public Accounts

### Recommendation

**10.12 Volume I should contain the Consolidated Financial Statements. The Operating Fund Financial Statements only relate to part of government operations and therefore should be included in Volume 2 of the Public Accounts with Crown agencies.**

### Special Projects Fund

**10.13** The Prince Edward Island Special Projects Fund was established under the Financial Administration Act effective March 31, 1999. Pursuant to the Act, the Lieutenant Governor in Council made regulations for the Fund. These Regulations established programs through which money can be disbursed, outlined the purpose of each program, determined eligibility criteria, and the approval and disbursement process.

**10.14** The Province's Operating Fund provided total grants of \$48 million to the Special Projects Fund; \$1 million in 2000-01 and \$23.5 million in each of the previous two years. When expenditures are approved by the Special Projects Fund for designated programs a transfer is made back to the Operating Fund. When expenditures are made on each project, they are appropriated through the Operating Fund. Following are the balance sheet and statement of revenue and expenditures for the Special Projects Fund for the past five years.

### SPECIAL PROJECTS FUND BALANCE SHEET

	Year Ended March 31 (Millions)				
	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>
Current Assets					
Due from Province	<u>\$3.4</u>	<u>\$16.3</u>	<u>\$23.6</u>	<u>\$40.9</u>	<u>\$23.5</u>
Fund Balance	<u>\$3.4</u>	<u>\$16.3</u>	<u>\$23.6</u>	<u>\$40.9</u>	<u>\$23.5</u>

## 10. Public Accounts

### SPECIAL PROJECTS FUND STATEMENT OF REVENUE, EXPENDITURES AND FUND BALANCE

	Year Ended March 31 (Millions)				
	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>
Provincial Grant-Operating Fund	\$ -	\$ -	\$ 1.0	\$23.5	\$23.5
Interest Income	<u>0.1</u>	<u>.6</u>	<u>1.9</u>	<u>1.0</u>	<u>-</u>
Total Revenues	0.1	.6	2.9	24.5	23.5
Expenditures	<u>13.0</u>	<u>7.9</u>	<u>20.2</u>	<u>7.1</u>	<u>-</u>
Excess Revenue (Expenditure)	(12.9)	(7.3)	(17.3)	17.4	23.5
Fund Balance, beginning of year	<u>16.3</u>	<u>23.6</u>	<u>40.9</u>	<u>23.5</u>	<u>-</u>
Fund Balance, end of year	<u>\$ 3.4</u>	<u>\$16.3</u>	<u>\$23.6</u>	<u>\$40.9</u>	<u>\$23.5</u>

**10.15** Expenditures were made by the following Funds within the Special Projects Fund in the past five years:

<u>Fund</u>	Year Ended March 31 (Millions)				
	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>
Health Care Stabilization Fund	\$ 9.6	\$3.7	\$ 6.2	\$1.6	\$ -
Development Fund	.3	1.0	9.3	3.4	-
Health Research Fund	.4	.3	.1	-	-
Sustainable Resource Support Fund	.6	-	1.2	1.3	-
Community Development Fund	1.0	.5	.9	.8	-
Education Stabilization Fund	<u>1.1</u>	<u>2.4</u>	<u>2.5</u>	<u>-</u>	<u>-</u>
Total	<u>\$13.0</u>	<u>\$7.9</u>	<u>\$20.2</u>	<u>\$7.1</u>	<u>\$-</u>

**10.16** The balance in the Special Projects Fund was \$3.4 million at March 31, 2003. Fund withdrawals of \$2 million were approved for 2003-04 in the Budget Estimates.

#### Outstanding Debentures and Related Accounts

**10.17** The largest single liability on the Province's financial statements is its outstanding debentures, which account for \$1.09 billion of the Province's \$1.9 billion liabilities. All of these debentures

## 10. Public Accounts

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have been issued in Canadian dollars. The outstanding debentures can be broken down into public and private issues of \$948.9 million and Canada Pension Plan issues of \$140.3 million. The public and private issues either have a sinking fund requirement or the balance is repaid over the term of the debenture. The Canada Pension Plan issues are issued for a 20 year period and do not contain sinking fund requirements.

**10.18** In September 2002, the Province issued a 25 year, \$100 million public debenture. The debenture carries an interest rate of 6.1 percent and will mature in July 2027. The contributions to the sinking fund for this issue are 1.25 percent per annum.

**10.19** At March 31, 2003, the Sinking Fund for debentures (\$171.5 million) and the Debt Reduction Fund (\$57 million) held combined net assets of \$228.5 million.

**10.20** The Debt Reduction Fund was established in June 2001 for the purpose of retiring debt and reducing interest costs. The activity of the Debt Reduction Fund for the year is as follows:

### DEBT REDUCTION FUND SUMMARY OF FINANCIAL ACTIVITY (Millions)

	<u>2002-03</u>
Balance, April 1, 2002	\$85.9
Investment Income	5.5
Payment of Debentures	<u>(34.4)</u>
Balance, March 31, 2003	<u>\$57.0</u>

**10.21** In previous years, we noted that a number of policy changes had occurred since the release of the Sinking Fund Investment Policy several years ago. We recommended that the Sinking Fund Investment Policy be updated and approved by Treasury Board to reflect all changes to policies that have occurred since the Policy was

## **10. Public Accounts**

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released. Management has completed a revised Sinking Fund Policy draft but it has not been reviewed and approved by Treasury Board.

## 10. Public Accounts

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### PEI Master Trust

**10.22** Investments of the Civil Service Superannuation, Teachers' Superannuation and MLA Pension Funds are consolidated into the Province of PEI Master Trust. Individual funds receive units in the Master Trust based on the net contributions and allocated shares of income and expense. The investments are managed by investment managers external to government and an external custodian is responsible for accounting and record keeping. An Investment Advisory Committee, with representation from government and plan members, provides assistance to Provincial Treasury with the investment of the Fund assets. The Fiscal Management Division of Provincial Treasury is responsible for overseeing the Master Trust.

**10.23** A new framework for investment of fund assets was developed and approved by Executive Council for implementation as of April 1, 2002. The new asset mix is based on a targeted 65/35 split between equities and fixed income investments while the previous asset mix had a targeted 60/40 split between equities and fixed income investments. The new investment framework provides for an increased percentage of investment in non-Canadian equities. The financial markets have improved since March 31, 2003, and at December 31, 2003, the pension fund assets balance as reported by the custodian was \$761.9 million. The following table provides a breakdown of the Master Trust Investments as of March 31, 2003 with comparative information at March 31, 2002. The balances combine balances invested with the Investment Managers and balances held in individual accounts of the participants.

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### PEI MASTER TRUST INVESTMENTS (Millions)

	Year Ended March 31	
	<u>2003</u>	<u>2002</u>
Accrued income	\$ 4	\$ 4
Canadian short term investments	10	66
Canadian bonds, debentures and notes	220	246
Canadian equity securities	243	314
Foreign equity securities	143	108
Canadian real estate	<u>6</u>	<u>6</u>
	<u>\$626</u>	<u>\$744</u>

**10.24** The investments totalling \$626 million include amounts which four of the five Master Trust fund managers have invested in their own pooled funds. The March 31, 2003 market values of these investments total \$227 million.

**10.25** The market value of the pension plan assets held by the Master Trust was \$626 million at March 31, 2003 compared to a market value of \$744 million at March 31, 2002. The following table illustrates the components giving rise to the decrease as well as the rate of return on trust assets.

### PEI MASTER TRUST CHANGE IN TRUST ASSETS (Millions)

	Year Ended March 31	
	<u>2003</u>	<u>2002</u>
Special contributions by Government	\$ 18	\$18
Interest and dividends	24	26
Market value gains(losses)	(140)	26
Plan withdrawals and expenses less contributions	<u>(20)</u>	<u>(5)</u>
Total increase(decrease)	<u>\$(118)</u>	<u>\$65</u>
Plan asset rate of return	<u>(15.4%)</u>	<u>7.3%</u>

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## 10. Public Accounts

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**10.26** An annual audit of the Master Trust is performed by our Office and our findings are reported to the Fiscal Management Division of Provincial Treasury. We expressed concerns regarding the adequacy of monitoring and control procedures in place for the Master Trust. Fiscal Management Division has conducted a review of procedures, and plan on taking action on the points raised.

### Public Sector Accounting Board (PSAB)

**10.27** PSAB is responsible for developing generally accepted accounting principles for the public sector. PSAB issues recommendations and guidance to serve the public interest by strengthening accountability in the public sector through developing, recommending, and gaining acceptance of accounting and financial reporting practices.

**10.28** There have been significant changes to the Province's financial statements over the years as a result of changes to address recommendations of the Public Sector Accounting Board of the Canadian Institute of Chartered Accountants. The 2002-03 fiscal year financial statements have for the most part been prepared in accordance with these recommendations. However, issues still remain to be addressed. The following comments summarize these issues.

#### *Tangible Capital Assets*

**10.29** In January 2003, PSAB approved a new reporting model for senior governments in Canada. This new PSAB Section is applicable for years beginning on or after April 1, 2005, although, earlier implementation is encouraged. The most significant change to the Province's financial statements is that tangible capital assets will be set up on the statement of financial position and amortized over their useful life on the statement of revenue and expenditure. This is a significant departure from the current accounting treatment where capital expenditures are expensed in their entirety on the Statement of Revenue and Expenditure in the year they are acquired and no value is recorded on the Statement of Financial Position. The proposed model will still highlight net debt but will include a value for

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## 10. Public Accounts

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tangible capital assets. The Province has indicated its intention to set up tangible capital assets on the statement of financial position as of March 31, 2005.

**10.30** Tangible capital assets are a significant economic resource managed by government and a key component in the delivery of many government programs. Providing complete information about tangible capital assets and the related amortization in the summary financial statements demonstrates stewardship and shows the cost of using those assets to deliver programs.

**10.31** The Public Accounts currently includes an unaudited schedule of tangible capital assets. The Province has indicated its intention to set up tangible capital assets on the statement of financial position as of March 31, 2005. In the past we identified a number of issues regarding the tangible capital asset schedule which need further examination. We have been advised that a number of adjustments have been made to costs in relation to the issues we identified and that work on the capital asset schedules is ongoing. We plan on completing our work on capital assets when the Province finalizes their work. Following are areas previously identified as requiring additional attention:

- Presently values provided for land are incomplete. Historical cost information or best estimates need to be gathered and reported for land.
- Differences were noted in the historical cost assigned to buildings in the Schedule of Tangible Capital Assets compared to costs recorded in the Public Accounts for the related buildings.
- Capital Expenditures for roads were being amortized at 10 percent on the declining balance basis. This area needs to be reviewed as some expenditures each year would be for repairs and maintenance to existing roads and not for the creation of new roads.
- The Draft Tangible Capital Asset Policy indicates that cost shall be net of any recoveries from other sources. We noted several instances where federal funding received for the purchase of various assets was not deducted from the total asset cost.

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## 10. Public Accounts

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### *Consolidated Budget Estimates*

**10.32** For many years, we have recommended that Government prepare Consolidated Budget Estimates rather than budgeting for the Operating Fund only. Since the Province's annual surplus or deficit is the main measure of financial performance, financial statement users should be given sufficient information to compare actual results to budget. The Consolidated Financial Statements with corresponding consolidated estimates would be a more complete document for understanding and assessing trends in government financial operations and would demonstrate public accountability for government's financial performance. Consolidated Budget Estimates were prepared for the first time for the 2003-04 year.

**10.33** PSAB Standards set as a basic requirement the inclusion of a consolidated budget with the Public Accounts. To facilitate meaningful comparisons, consolidated budgets need to be prepared and reported on the same basis as that used to prepare the Consolidated Financial Statements. The 2003-04 Budget Estimates were prepared on a consolidated basis but we noted differences between the format used in the Budget and the basis used in the 2002-03 Consolidated Financial Statements. This will create difficulties in providing budget to actual comparison in the Public Accounts. It is our understanding that an alternative presentation will be followed in future years. To facilitate comparability, it is important that the budget figures be prepared on the same basis as the actual results.

### *Timely Financial Statements*

**10.34** We continue to stress the importance of releasing the Public Accounts on a timely basis. Financial statements are an important source of information for decision makers. Their usefulness diminishes as time elapses and increased efforts are needed to have financial statements available on a more timely basis. The following schedule provides the dates that the Consolidated (Summary) Financial Statements for the years ended March 31, 2001, 2002, and 2003 were released for each jurisdiction in Canada.

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### CONSOLIDATED (SUMMARY) FINANCIAL STATEMENTS RELEASE DATES YEAR ENDED MARCH 31

<u>Jurisdiction</u>	<u>2003</u>	<u>2002</u>	<u>2001</u>
Newfoundland and Labrador	Nov. 18, 2003	Nov. 25, 2002	Nov. 28, 2001
Nova Scotia	Nov. 13, 2003	Dec. 20, 2002	Nov. 16, 2001
Prince Edward Island	Dec. 10, 2003	Jan. 30, 2003	Jan. 31, 2002
New Brunswick	Nov. 21, 2003	Oct. 04, 2002	Oct. 01, 2001
Quebec	*	Dec. 18, 2002	Dec. 14, 2001
Ontario	Nov. 21, 2003	Nov. 07, 2002	Sept. 21, 2001
Manitoba	Sept. 30, 2003	Sept. 30, 2002	Sept. 28, 2001
Saskatchewan	July 21, 2003	Aug. 01, 2002	July 20, 2001
Alberta	June 24, 2003	June 25, 2002	June 28, 2001
British Columbia	June 27, 2003	July 11, 2002	Aug. 09, 2001
Canada	Nov. 04, 2003	Oct. 15, 2002	Sept. 27, 2001

\*Not released as of Jan. 31, 2004.

**10.35** The Financial Administration Act requires each reporting entity to have audited financial statements completed within three months of year end and an annual report available to the public within six months of year end. Some entities, such as the Civil Service Pension Fund and the MLA Pension Funds, are not completing their financial statements on a timely basis.

#### **Recommendation**

**10.36 The Public Sector Accounting Board recommendations related to tangible capital assets, consolidated budget estimates, and timely financial statements, should be followed.**

#### **Pension Obligation**

**10.37** A pension obligation arises when the pension entitlements owed to employees for services rendered exceed pension fund assets. The Province recorded this obligation in the Public Accounts for the first time on March 31, 1994. The amount of the obligation at that time was \$345 million. To address this problem in 1995-96, the

## 10. Public Accounts

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Province made the first payment on the \$197 million in additional funding to be provided over ten years to the Teachers' and Civil Service Superannuation funds. The last additional payments to the Teachers' and Civil Service Superannuation Funds of \$12.1 million and \$5.9 million respectively will be made on April 1, 2004. The additional payments, along with high rates of return on pension fund investments and increased contribution rates, helped reduce the obligation to \$126.4 million at March 31, 1998. However, pension plan amendments and declining investment returns have caused this trend to be reversed.

**10.38** The Public Accounts have reported the following total pension obligations during the past five years:

	Year Ended March 31				
	(Millions)				
	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>
Pension fund liabilities	\$955.6	\$898.7	\$909.2	\$858.4	\$732.1
Pension fund assets	<u>626.6</u>	<u>744.8</u>	<u>680.4</u>	<u>656.0</u>	<u>574.3</u>
Unfunded Pension Liability	<u>\$329.0</u>	<u>\$153.9</u>	<u>\$228.8</u>	<u>\$202.4</u>	<u>\$157.8</u>

**10.39** Decreases in pension assets of \$118.2 million have resulted in a significant increase in the unfunded pension liability at March 31, 2003. The pension fund assets decreased from \$744.8 million at March 31, 2002 to \$626.6 million at March 31, 2003. The financial markets have improved since March 31, 2003, and at December 31, 2003, the pension fund assets are reported by the custodian at \$761.9 million.

**10.40** Pension obligations are calculated on an actuarial basis every three years. During the interim period, liabilities are estimated by the province by extrapolating the data from the most recent valuation. Projections were used in calculating the liabilities at March 31, 2003. Actuarial valuations were carried out for the Teachers' Superannuation Fund and the Civil Service Superannuation Fund as of April 1, 2002 and for the MLA Pension Funds as of April 1, 2003. The following values were reported by the actuary as of the valuation dates:

## 10. Public Accounts

	(Millions)			
	TSF	CSSF	Prior MLA	New MLA
Date of Valuation	Apr.1/02	Apr. 1/02	Apr. 1/03	Apr.1/03
Pension fund liabilities	\$440.6	\$442.2	\$12.5	\$2.0
Pension fund assets	<u>287.0</u>	<u>436.1</u>	<u>16.3</u>	<u>1.6</u>
Pension Obligation	<u>\$153.6</u>	<u>\$ 6.1</u>	<u>\$ (3.8)</u>	<u>\$ .4</u>

**10.41** The Public Accounts report the following pension obligations for the Teachers' Superannuation Fund (TSF); Civil Service Superannuation Fund (CSSF); MLA Pension Funds (MLA); and other Pension Plans at March 31, 2003:

	Year Ended March 31, 2003					
	(Millions)					
	TSF	CSSF	Prior Plan MLA	New Plan MLA	Other	Total
Pension fund liabilities	\$459.5	\$469.7	\$12.5	\$2.0	\$11.9	\$955.6
Pension fund assets	<u>235.7</u>	<u>373.0</u>	<u>16.3</u>	<u>1.6</u>	<u>-</u>	<u>626.6</u>
Gross Pension Obligation	<u>\$223.8</u>	<u>\$ 96.7</u>	<u>\$ (3.8)</u>	<u>\$ .4</u>	<u>\$11.9</u>	<u>\$329.0</u>

**10.42** The Teachers' Superannuation Fund accounts for approximately 68 percent of the province's total pension obligation. Given the magnitude of the \$223.8 million unfunded liability of the Teachers' Superannuation Fund, and the fact that government will be making its last additional required payment of \$12.1 million on April 1, 2004, a long term plan to address this liability is required. Provincial Treasury is currently reviewing this issue.

<b>Recommendation</b>
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<b>10.43</b> A long term plan to address the unfunded liability of the Teachers' Superannuation Fund is required.
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## 10. Public Accounts

### Federal Revenue

**10.44** During the course of our audit of the Public Accounts for the year ended March 31, 2003, the Province received notice of reduced entitlements to Equalization and Canada Health and Social Transfer (CHST) revenues. These adjustments included reduced Equalization entitlements totalling \$16.8 million and reduced CHST entitlements totalling \$4.2 million for fiscal years ended March 31, 2003 and prior years. These amounts were recorded as reductions of 2002-03 revenues.

**10.45** We have commented in past years on problems with timely receipt of amounts due from the federal government. During 2002-03, receivables from the federal government, excluding transfer payments, increased from \$22.8 million as at March 31, 2002 to \$26.7 million as at March 31, 2003. Of the \$26.7 million receivable as at March 31, 2003, \$9.9 million remained outstanding as at December 31, 2003. The following table summarizes six individual balances greater than \$1.0 million which account for \$21.6 million, or 81 percent of the \$26.7 million outstanding as at March 31, 2003.

#### FEDERAL RECEIVABLES GREATER THAN \$1.0 MILLION AS AT MARCH 31, 2003 (\$000)

	Receivable	Receipts	Outstanding
	<u>Mar. 31/03</u>	<u>Apr. 1/03 to Dec. 31/03</u>	<u>Dec. 31/03</u>
Promotion of Official Languages	\$ 4,843	\$ 1,794	\$3,049 Note(1)
Infrastructure Program	2,226	2,226	0
Skills Development	3,924	3,924	0
Official Languages in Education	6,356	3,682	2,674 Note(2)
Primary Health Care Transition Fund	1,841	1,841	0
Youth Justice Services and Programs	<u>2,390</u>	<u>100</u>	<u>2,290</u> Note(3)
	<u>\$21,580</u>	<u>\$13,567</u>	<u>\$8,013</u>

(1) 2001-02 \$1,487; 2002-03 \$1,562;  
 (2) 2000-01 \$ (114); 2001-02 \$696; 2002-03 \$2,092;  
 (3) 2002-03 \$2,290;

## 10. Public Accounts

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**10.46** During the year we conducted an examination of Federal Claims related to Federal/Provincial Contribution Agreements. Additional comments and recommendations related to Federal Claims are in the Special Audits and Examinations Section of this Report.

### Recommendation

**10.47 Steps should be taken to ensure all revenues from the federal government are claimed and received on a timely basis.**

### Guaranteed Debt

**10.48** Over the past five years the Province has reported the following guaranteed debt balances on the guaranteed debt schedule.

	Year Ended March 31				
	(Millions)				
	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>
Guaranteed Debt	<u>\$83.1</u>	<u>\$47.2</u>	<u>\$42.9</u>	<u>\$27.6</u>	<u>\$24.5</u>

Guarantees have increased by \$58.6 million since 1999. Of this, \$39.6 million relates to guarantees to Crown Corporations. Guarantees were provided to Island Waste Management Corporation on financing relating to implementation of the Island Waste Watch program and facilities (\$29.7 million) and to PEI Energy Corporation on financing relating to the Wind Farm Project (\$8.3 million).

**10.49** Guarantees to business organizations at March 31, 2003 accounted for \$21.1 million of the total guarantees and have increased by \$9.4 million since 1999. These guarantees include a \$12 million guarantee to Polar Foods.

**10.50** In 2001, as a result of changes in the student loan program, the Province began guaranteeing all student loans issued through the PEI Student Loans Program. Guarantees under the new Student Loans program were \$8.3 million at March 31, 2003.

## 10. Public Accounts

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**10.51** Over the five year period, guarantees have been provided on financing of a number of Community based projects. The guaranteed balances for Community based programs are \$1.3 million at March 31, 2003.

**10.52** The Province has included provisions for losses of \$7.8 million on the guarantees. Schedule 21 of the Public Accounts shows a continuity schedule for the Provision for Doubtful Accounts. The Provision for Doubtful Accounts for Loan Guarantees has increased from \$1.9 million at March 31, 2002 to \$7.8 million at March 31, 2003. With the rising dollar value of guarantees being issued, it is important that the Province perform a detailed review of all guarantees each year and ensure a reasonable provision for losses is established at year end.

**10.53** In addition to the balances noted above, note 6(b) to the Consolidated Financial Statements provides information on the guarantee to the Credit Union Deposit Insurance Corporation and note 6(d) provides information on the guarantee to the Minister of Citizenship and Immigration. These guarantees have been disclosed in the Public Accounts notes but have not been included on the guaranteed debt schedule in the Public Accounts.

### **Cancellation or Discharge of Debt**

**10.54** Section 16 of the Audit Act requires the Auditor General to report the total amount of any claims, debts or monies due to the Province that have been discharged, cancelled, and released under Section 26 of the Financial Administration Act. In 2002-03, the amount cancelled or discharged under Section 26 totalled \$7,423,136 and the amount written off under Section 26.1 was \$7,099,162 as follows:

## 10. Public Accounts

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	Section 26(1)	Section 26.1(1)
Real Property Tax Act	\$ 13,091	\$ 133,082
Gasoline Tax Act	-	2,302
Revenue Tax Act	-	973,931
Financial Administration Act	-	161,342
Welfare Assistance Act	8,085	-
PEI Business Development Inc.	5,106,860	5,768,860
Lending Agency Act	2,295,100	55,245
Public Health Act	-	4,400
	<u>\$7,423,136</u>	<u>\$7,099,162</u>

The net amount discharged, cancelled and released or written off owed by third parties to the Province was \$9,415,438. The amounts relating to the PEI Business Development Inc. include a write-off of debts owed by various businesses to the PEI Business Development Inc. in the amount of \$5,768,860 and a corresponding cancellation of amounts owed by the PEI Business Development Inc. to the Province in the amount of \$5,106,860.

### Surplus (Deficit) of Crown Agencies and Corporations

**10.55** Section 16 of the Audit Act requires the Auditor General to include information in the Annual Report on deficits of agencies not covered by appropriations in the year in which they have been incurred, and any surpluses not paid into the Operating Fund in the year in which they are earned. For information purposes we have also included the cumulative surplus or deficit for each entity.

## 10. Public Accounts

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<b>AGENCY</b>	<b>Annual Surplus(Deficit) For the Year</b>	<b>Cumulative Surplus (Deficit)</b>
Agricultural Insurance Corporation	\$ 3,152,472	\$ 5,523,834
Agricultural Research Investment Fund Inc.	70,385	1,304,412
Aquaculture and Fisheries Research Initiative Inc.	46,775	847,052
Business Development Inc.	416,066	1,620,553
Charlottetown Area Development Corporation	(173,589)	4,749,599
Eastern School District	46,002	46,002
Energy Corporation	663,655	1,309,534
French Language School Board	(997)	58,945
Grain Elevators Corporation	20,624	386,797
Human Rights Commission	(3,648)	-
Innovative Solutions Agency (PEI) Inc.	(46,554)	-
Island Investment Development Inc	206,616	4,361
Island Waste Management Corporation	(179,000)	(609,506)
Lending Agency	(2,204,621)	(1,376,497)
Museum and Heritage Foundation	(119,457)	565,696
Self-Insurance Fund	(110,349)	7,908,460
Special Projects Fund	(12,902,604)	3,381,315
Summerside Regional Development Corporation Ltd.	(321,904)	1,619,031
Tourism PEI	(84,260)	(167,044)
Western School Board	23,362	23,362
Workers Compensation Board	4,272,096	(25,647,162)

### MANAGEMENT RESPONSE

**10.56** These matters have been discussed with management.

# 11. APPROPRIATIONS

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## INTRODUCTION

**11.1** Our audit of Appropriations for the year ended March 31, 2003 included a review of the systems and procedures for the administration of the Province's annual budget. This required an audit of appropriations approved by the Legislature and special warrants approved by Executive Council on the recommendation of Treasury Board.

**11.2** The Appropriations Act provides the spending authority for government and is approved by the Legislative Assembly annually. Appropriations for 2002-03 were approved in the Appropriation Act 2002. If additional funds are required during the year, special warrants are issued by the Lieutenant Governor in Council.

**11.3** In **SCHEDULE A** attached to this report, we provide a comparison of appropriations to actual expenditures in accordance with the classifications in the Appropriation Act 2002.

## SPECIAL WARRANTS

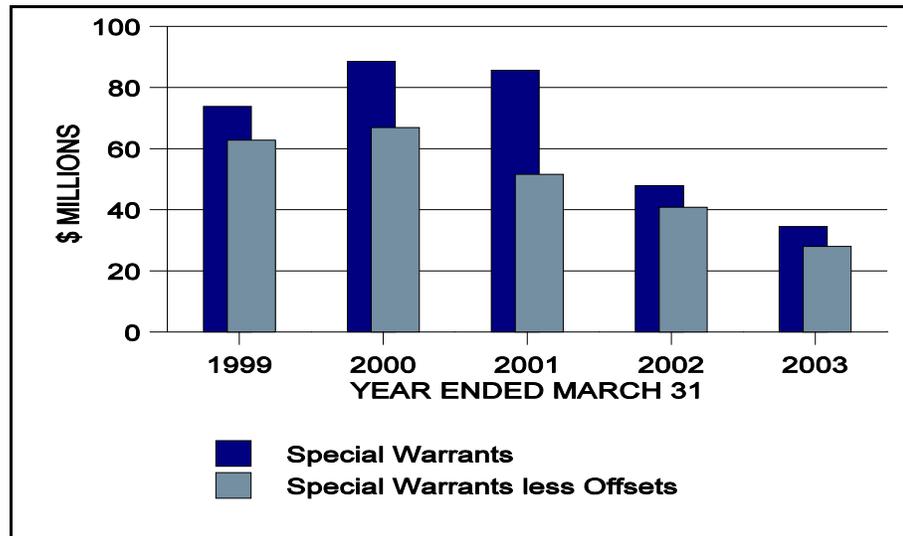
**11.4** Section 16(h) of the Audit Act requires the Auditor General to list in detail appropriations made by special warrant and the purpose of such appropriations. Details are shown in **SCHEDULE B** attached to this report.

**11.5** For the 2002-03 fiscal year, special warrants totalled \$34.5 million compared to \$47.9 million issued for 2001-02. Of the special warrants issued for 2002-03, \$6.3 million was offset by revenue and \$0.3 million was offset by funds sequestered from appropriations. The result was a net increase in provincial appropriations of \$27.9 million.

**11.6** **Exhibit 11.1** indicates the gross special warrants and special warrants net of any offsets for the last five years.

## 11. Appropriations

**EXHIBIT 11.1  
SPECIAL WARRANTS**



**11.7** Normally no expenditure should be incurred unless it is provided for by an appropriation. At year end, adjustments may be necessary to ensure the financial statements present fairly the revenues and expenditures of the Province. When this occurs, it would be expected that a special warrant would be issued on a timely basis for any over expenditures. We noted a delay in preparing special warrants for year end adjustments.

### Recommendation

**11.8** Special warrants should be issued on a timely basis.

### Transfers

**11.9** Section 37.2 of the Financial Administration Act which was assented to on May 10, 2002, provides for the transfer of salary increases from General Government to the various government entities. Section 37.2 states

- (1) "When the Treasury Board has approved collective agreements which include salary increases for public sector employees, the Lieutenant Governor in Council may approve the transfer of monies appropriated to general government for such purposes

## 11. Appropriations

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and to such departments listed in Schedule A or to Crown corporations listed in Schedule B, as it considered appropriate.”

- (2) “The Provincial Treasurer shall report all transfers of monies pursuant to subsection (1) to the Legislative Assembly as soon as practicable.”

We noted that transfers totalling \$4.8 million were not approved by an Order In Council. It should be clarified whether an Order In Council is necessary to transfer an appropriation vote.

### **Recommendation**

**11.10 A review of Section 37.2 of the Financial Administration Act should be carried out to ensure the appropriate documentation is being prepared for appropriation transfers.**

### **MANAGEMENT RESPONSE**

**11.11** We have discussed our findings with management.



## **UPDATE ON PREVIOUS RECOMMENDATIONS**



## 12. UPDATE ON PREVIOUS RECOMMENDATIONS

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### INTRODUCTION

**12.1** At the conclusion of each special audit, we provide an audit report including recommendations designed to improve the management and administration of government operations and programs. It is management's prerogative to select the best course of action to address the problems identified. We are primarily concerned that all recommendations are being addressed by management.

**12.2** Each year, we request information from departments and agencies on the status of action taken to address outstanding recommendations. Normally this information consists of correspondence from the Deputy Minister or Chief Executive Officer of the organization. We do not always further verify or check the information received, however, we do review the responses for reasonableness. In most cases it is more cost-effective to do detailed verification during the next scheduled audit.

**12.3** Following is summary information provided to us on the status of recommendations from the special audits and examinations reported in the 2003 Annual Report of the Auditor General as well as outstanding recommendations from audits in the 2002 Annual Report.

## 12. Update on Previous Recommendations

### The Governance Structure of the Credit Union Deposit Insurance Corporation under the Regulatory Framework for Credit Unions

**12.4** Following are the recommendations resulting from our review of the Governance Structure of the Credit Union Deposit Insurance Corporation under the Regulatory Framework for Credit Unions as presented in the 2003 Annual Report of the Auditor General. The status of implementation of the recommendations is provided based on information received from the Office of the Attorney General.

<b>Auditor General's Recommendation</b>	<b>Status/Management Response</b>
The Credit Unions Act should be revised to require Board members to hold office for a specified term.	The Office of the Attorney General plans to put forward proposed amendments to the Credit Unions Act in the fall of 2004.
Eligibility requirements for the appointment of members to the Board of Directors of the Credit Union Deposit Insurance Corporation should be established and should specifically exclude employees of credit unions, Credit Union Central, and CUDIC.	The Office of the Attorney General plans to put forward proposed amendments to the Credit Unions Act in the fall of 2004.
Guidelines on the desirable qualifications and attributes of prospective Board members should be developed and considered in the nomination process.	The Attorney General's office supports this recommendation and will consider it after legislative changes are addressed.
The Board should establish a process for periodic review of the role and function of the Board in fulfilling its responsibilities under the Credit Unions Act.	The Board of CUDIC concurs that board review is important.
The Board of the Credit Union Deposit Insurance Corporation should document approved policies in a policy manual and update the manual as required.	The Board of CUDIC agrees with this recommendation. It is considering hiring its own staff to address a number of issues.

## 12. Update on Previous Recommendations

Auditor General's Recommendation	Status/Management Response
The Credit Unions Act should be amended to provide an inspection function that is controlled by the Credit Union Deposit Insurance Corporation.	The Office of the Attorney General supports this recommendation and advised that they are seeking the views of the various parties in the system.
The Board of Directors of the Credit Union Deposit Insurance Corporation should meet regularly to review monitoring information on the credit unions.	CUDIC agrees with this recommendation.
The Board of Directors of the Credit Union Deposit Insurance Corporation should develop a Board policy which sets out actions to be taken for certain categories of risk associated with deteriorating financial condition of a credit union.	The Board of CUDIC supports this recommendation.
Each credit union should be subject to an annual external financial audit. The Credit Unions Act should be amended to require a credit union auditor to be a public accountant as defined under the Public Accounting and Auditing Act.	The CUDIC Board and the Office of the Attorney General are working to gain support within the credit union system on this recommendation. Amendments to the Credit Unions Act will be considered.
The Board of Directors of the Credit Union Deposit Insurance Corporation should re-examine the investment policy for the deposit insurance fund and consider introducing diversification into the portfolio.	The Board of CUDIC agrees with this recommendation.
The annual report of the Credit Union Deposit Insurance Corporation should include additional information resulting from the monitoring of credit unions and the administration of the Deposit Insurance Fund.	CUDIC agrees with this recommendation.

## 12. Update on Previous Recommendations

### HIGHWAY MAINTENANCE

**12.5** Following are the recommendations resulting from our audit of the Highway Maintenance Division of the Department of Transportation and Public Works as presented in the 2003 Annual Report of the Auditor General. The status of implementation of the recommendations is provided based on information received from management of the Department.

<b>Auditor General's Recommendation</b>	<b>Status/Management Response</b>
The Highway Maintenance Division should prepare a plan which sets out measurable objectives. The annual report should show the results achieved compared to the objectives.	The Division is developing a plan which will set out measurable objectives. The annual report will be reformatted to show results achieved once the plan is implemented.
The priority patching plans should be formally approved by the County Superintendents.	Implemented.
The priority patching plans should be entered into the management information system to assist in monitoring the work of the patching crews.	A monitoring program has been established.
The County Superintendents should monitor the information provided on the priority patching plans and obtain explanations for any deviations from the plan.	Superintendents reviewed priority patching progress throughout the patching season and provided direction to supervisors and work crews as required.
When assessing the performance of zone crews, the Division should review both productivity and quality. Where targets are not being achieved, the reasons should be determined and corrective action taken.	Targets have been established with follow-up to ensure targets were met. This was carried out by Superintendents and the Division's Technical Services Coordinator.

## 12. Update on Previous Recommendations

Auditor General's Recommendation	Status/Management Response
<p>The recapping of paved roads should be prioritized by county rather than the current practice of allocating approximately the same resources among the electoral districts.</p>	<p>Overall needs are great and the current programming meets approximately one-third of these needs. The present system is a reasonable approach. The Department continues to monitor to ensure the prioritization of the recap program provides a responsible outcome.</p>
<p>Prior to contracting recapping work, a cost analysis should be prepared demonstrating the benefit to government.</p>	<p>Carried out.</p>
<p>As required by Treasury Board Policy on signing authority, contracts over \$100,000 should be approved by Treasury Board.</p>	<p>The Department accepts and follows the requirements of Treasury Board.</p>
<p>The Division should prepare and implement a plan for roadside maintenance which identifies the maintenance activities required by zone, provides a work schedule to address these requirements, and allocates resources based on the plan and work schedule.</p>	<p>The Department agrees in general terms. By nature, the work carried out by highway maintenance crews is reactive and makes it very difficult to adhere to a pre-season schedule. However, short term, week-to-week planning at the Supervisor/Foreman level has been strengthened and will continue to be strengthened.</p>
<p>The Division should determine the labour required to carry out summer maintenance activities as established in a Divisional plan. Management should prepare a summary showing variances from the plan and provide explanations for any differences.</p>	<p>The Department will be undertaking a review of resource requirements based on past activities and will take steps to establish a summer maintenance plan with measurable objectives.</p>

## 12. Update on Previous Recommendations

Auditor General's Recommendation	Status/Management Response
The Division should determine the reasons for the lower cost of snow clearing secondary roads in Kings County and take action to address any opportunities to reduce costs in other counties.	A review is underway and information should be available prior to next winter's maintenance season.
The Division should re-examine the benefit and cost of using wingmen on truck plows.	A review is being conducted.
The Division should ensure that Treasury Board approval is obtained for the rate package negotiated with the Road Builders Association for snow clearing contracts.	Implemented.
The Division should ensure that equipment requirements outlined in contracts are adhered to and any deficiencies in contractor equipment are corrected.	Implemented and strengthened.
The Division should follow up on the high application rate for salt, and take corrective action if necessary.	All equipment scheduled to spread salt has been equipped with computer spreader equipment. Salt applications will be monitored and corrective action taken as required.
Highway Maintenance Division should monitor annual sand usage of contractors and ensure significant deviations from normal use are explained.	A new monitoring program is being developed. Contractors will be advised if deviations from normal use are found.
Highway Maintenance Division should examine the feasibility of converting snow clearing and sanding contracts into combination contracts on suitable routes.	The latest snow and sanding contracts are established to end in 2006. This will allow the Department time to implement combination contracts where practical.

## 12. Update on Previous Recommendations

Auditor General's Recommendation	Status/Management Response
The Division should update the plan for replacement of equipment. Forecast needs and an evaluation of what equipment is most suitable to meet those needs should be considered.	This planning process has been strengthened and will be updated as required.
The Division should conduct a detailed analysis of the need for light vehicles including crew, materials and equipment transport.	A committee has been established to address this recommendation.
The Division's policy for half-ton rentals from employees should be submitted to Treasury Board for review and approval.	Prior to this year's summer maintenance season, the Division intends to have a submission to Treasury Board for review.
Leasing arrangements which result in an uneconomic use of Division resources should be avoided.	Agreed. No new lease arrangements have been entered into in the past year.
Equipment should be purchased in accordance with the requirements of the Public Purchasing Act.	Agreed. No equipment has been purchased outside of the Public Purchasing Act this year.
All lease purchase arrangements should be documented and formally approved in an agreement.	Agreed.
To assist in monitoring costs of the equipment fleet, the Division should utilize the costing reports which can be produced by the FleetAnywhere System.	This particular application of this system is presently under review to ensure that reporting provides cost information which will improve management of the equipment fleet.
The Auto Shop Supervisors should monitor preventive maintenance services being provided to ensure compliance with the Division's policy on preventive maintenance.	All Mechanical Branches now comply.

## 12. Update on Previous Recommendations

<b>Auditor General's Recommendation</b>	<b>Status/Management Response</b>
Work orders and preventive maintenance checklists should be signed by mechanics and included with vehicle files.	The Mechanical Branches are presently setting up equipment files to comply with the National Safety Code which will address this item.
The Division should compare the cost of renting each type of equipment with the cost of owning equipment to determine whether renting or owning is more economical.	A review will be undertaken.
The Division should consider using a dispatch system for utilizing dump trucks during the summer.	Further review of using a dispatch system will be undertaken.
The Division should comply with Treasury Board's Travel Policy.	Methods to strengthen the ability to comply are to be undertaken.

## 12. Update on Previous Recommendations

### INFRASTRUCTURE PROGRAM

**12.6** Following are the recommendations resulting from our audit of the Infrastructure Program as presented in the Auditor General's 2003 Annual Report. The status of implementation of the recommendations is provided based on information received from management of the Department of Community and Cultural Affairs.

Auditor General's Recommendation	Status/Management Response
The Management Committee should approve annual audit plans as outlined in the Program Agreement.	To date, the Management Committee has not approved audit plans. It was decided that the standard audit plan for ACOA projects will be adopted after any appropriate changes are made.
The Management Committee should obtain clarification on the method for calculating investment targets.	The method of calculating investment targets is still under discussion. ACOA received a verbal agreement at a national meeting that the method would be amended to use only the Federal/Provincial share of costs, and that a letter would be forthcoming to that effect. The Province also received a verbal opinion from Infrastructure National Office that the change could be made. The matter will be settled prior to implementation of the Municipal Rural Infrastructure Fund (MRIF) next year.
The Management Committee should ensure that the rationale for approving projects is documented.	The Joint Secretariat continues to work on development of rationale for approval of projects.
All approved projects should be supported with complete applications including adequate supporting documentation.	Management Committee continues to strive to educate applicants on what constitutes sufficient documentation. The Program Secretariat makes every effort to obtain full details on all applications, but many communities simply do not have the expertise in place to provide the necessary data.

## 12. Update on Previous Recommendations

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<b>Auditor General's Recommendation</b>	<b>Status/Management Response</b>
The Program Manager should follow up with applicants to obtain the required documentation as outlined in their Funding Agreement.	The Program Manager has instituted new policies in order to ensure that applicants provide necessary documents prior to receiving funds.
Adequate cost data should be obtained from applicants and used as a basis for processing claims and monitoring projects.	Projects are now being more closely scrutinized to ensure that tender documents, quotations, change orders, etc., are supplied by the project managers.

## 12. Update on Previous Recommendations

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### VERIFICATION OF THE PRINCE EDWARD ISLAND REPORT ON COMMON HEALTH INDICATORS

**12.7** Our office verified the Prince Edward Island Report on Common Health Indicators, which was prepared by the Department of Health and Social Services. We performed specified auditing procedures and the 2003 Report of the Auditor General included one recommendation. The status of implementation of the recommendation was provided by management of the Department.

<b>Auditor General's Recommendation</b>	<b>Status/Management Response</b>
The Department should ensure that data is collected on all the measures required to be reported by PEI in comparable health indicator reports.	Management indicated that not all measures apply to PEI and some data is not available.

## 12. Update on Previous Recommendations

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### INVENTORY

**12.8** The recommendation resulting from the audit of Inventory follows. The recommendation was reported in the 2003 Annual Report of the Auditor General. The status of implementation of this recommendation is provided by management of the Department of Transportation and Public Works.

<b>Auditor General's Recommendation</b>	<b>Status/Management Response</b>
The Department of Transportation and Public works should take steps to reduce inventory levels of bridge materials, government garage parts, and sign shop materials.	Steps have been taken to strengthen tracking of culvert inventory levels. An exercise is presently underway to establish a system to ensure appropriate levels of inventory of parts at the Mechanical Branches. Inventory levels will be monitored and adjusted according to the delivery of materials for the sign shop.

## 12. Update on Previous Recommendations

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### EQUIPMENT

**12.9** The recommendations resulting from the audit of Equipment follow. These recommendations were reported in the Auditor General's 2003 Annual Report. The status of implementation of these recommendations as provided by management of the departments is also presented.

<b>Auditor General's Recommendation</b>	<b>Status/Management Response</b>
As required by Treasury Board policy, departments should complete an annual inventory count of equipment.	Most departments indicated annual inventory counts will be completed.
When updating inventories, the inventory count should be compared against previous inventory records and purchases. Any discrepancies should be followed up and explained.	Inventory counts will be compared with previous records when they are available.
In accordance with Treasury Board policy, departments should maintain complete records of all furniture and equipment.	Complete records will be maintained as inventory counts are completed.
Departments should review procedures for protecting equipment against loss or damage.	Staff are encouraged to ensure equipment is protected against loss or damage.

## 12. Update on Previous Recommendations

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### LOANS UNDER THE IMMIGRANT INVESTOR PROGRAM

**12.10** Following is an outstanding recommendation resulting from our audit of Loans Under the Immigrant Investor Program as presented in the Auditor General's 2002 Annual Report. Information received from management of Island Investment Development Inc. on the current status of this recommendation follows.

<b>Auditor General's Recommendation</b>	<b>Status/Management Response</b>
Information should be provided annually to government and the Legislature summarizing the exposure to the Province under the Immigrant Investor Program.	An annual report for fiscal 2002-03 has been prepared.

## 12. Update on Previous Recommendations

### PEI BUSINESS DEVELOPMENT INC. GRANTS AND CONTRIBUTIONS

**12.11** Following are the outstanding recommendations resulting from our audit of PEI Business Development Inc. Grants and Contributions presented in the Auditor General's 2002 Annual Report. The current status of implementation of the recommendations is provided based on information received from management of PEI Business Development Inc.

<b>Auditor General's Recommendation</b>	<b>Status/Management Response</b>
The Board of Directors should fulfil its responsibility to conduct the affairs of the corporation as required by legislation.	A new Board of Directors was appointed and the first meeting was held in November 2003.
The Board of Directors should establish Board policies around key aspects of the organization such as Board/management responsibility, reporting requirements of the Board, the establishment of performance targets, and approval of plans and budgets.	At the November meeting, the Board of Directors discussed board policies, board responsibility, reporting requirements and performance targets.
The strategic plan for PEI Business Development Inc. should be formally approved by the Board of Directors.	The current year's plan has been approved by the Board of Directors.
Progress against the targets established in the plan should be reported to the Board of Directors on a periodic basis.	Measurements are under development.
Actual job creation should be determined on a periodic basis and reported to the Board of Directors.	Measurements for actual job creation are under development.
PEI Business Development Inc. should monitor financial information to ensure that the terms of the Letter of Offer are followed by the client.	Monitoring of financial information is the responsibility of the project officer. Management was considering creating a new position to centralize some of this work. Management will seek direction from the Board of Directors on this issue.

## 12. Update on Previous Recommendations

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<b>Auditor General's Recommendation</b>	<b>Status/Management Response</b>
Criteria should be developed for all programs and approved by the Board of Directors.	Criteria have been developed and will be brought forward for board approval in the near future.
Policies and procedures should be established to ensure appropriate control and accountability over loans including; approvals, security requirements, interest subsidies, monitoring, and collections.	Approved policies are being followed.

## 12. Update on Previous Recommendations

### ACCOMMODATIONS

**12.12** Following we present the outstanding recommendations resulting from the audit of Accommodations presented in the Auditor General's 2002 Annual Report. The status of implementation of these recommendations is presented based on information received from management of the Department of Transportation and Public Works.

<b>Auditor General's Recommendation</b>	<b>Status/Management Response</b>
The Section should require departments to use an accommodations request form that clearly details all pertinent information regarding the space requirements.	The form is currently under revision.
In accordance with Treasury Board Policy, the Section should develop accommodations and office furniture standards for review and approval by Treasury Board.	Draft standards have been prepared and are currently being tested.
The Section should prepare a plan containing long term objectives for space usage.	The Section has prepared a summary of departments' needs and intends to meet with deputy ministers to address outstanding issues.
Where a lease agreement requires the landlord to provide a statement of operating costs, the Section should obtain the statements. The statements should be assessed for reasonableness and the amounts paid for operating costs should be supported by appropriate documentation.	The Section is attempting to obtain statements for base year costs and requires supporting documentation be provided before paying operating costs.
Approval should be obtained from Treasury Board or Executive Council for the practice of subleasing space on a rent free basis to non-government groups. In cases where property is subleased, the arrangements should be documented in a lease agreement.	Management indicated that this recommendation will be coming into effect for all of these arrangements when leases are being renegotiated.

## 12. Update on Previous Recommendations

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<b>Auditor General's Recommendation</b>	<b>Status/ Management Response</b>
Transportation and Public Works should approve all tenants before they move into the Royalty Centre. The rentals rates and terms should be documented in agreements.	A lease/operating agreement has been signed with Sport P.E.I. The agreement establishes a joint management committee which will address issues that arise.

## 12. Update on Previous Recommendations

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### EMPLOYMENT DEVELOPMENT AGENCY

**12.13** The recommendations which had not been fully addressed at the time of the 2003 Annual Report of the Auditor General were followed up again this year. Following is the status of implementation of these recommendations as provided by management of the Employment Development Agency.

<b>Auditor General's Recommendation</b>	<b>Status/Management Response</b>
The Board of Directors should meet on a regular basis to conduct the affairs of the Agency as required under the Employment Development Agency Act.	Management indicated that the Board met in November 2003.
Documentation should be maintained to demonstrate that eligibility criteria were considered before the projects were approved.	Program officers review the applications against the criteria and make a recommendation. Successful applicants are notified and applicants who are not successful are provided with the reasons for non-approval.
Project sponsors should be required to submit a summary of project results, including a statement of the original objectives and the results achieved. This information should be considered in the selection criteria for future projects submitted by the project sponsor.	Management indicated that a letter has been forwarded to sponsors requesting a written summary of project results including a statement of the original objectives and the results achieved.



**PUBLIC ACCOUNTS COMMITTEE**



## **13. PUBLIC ACCOUNTS COMMITTEE**

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### **ROLE AND MANDATE**

**13.1** The Standing Committee on Public Accounts is a Committee of the Legislative Assembly. It provides an important link in the accountability process. Through the Committee proceedings members of the Committee, as members of the Legislative Assembly, are given the opportunity to hold the administration accountable for the use of public funds and the stewardship of public assets.

**13.2** The Committee currently consists of eight members and is chaired by a member of the Official Opposition. Its responsibility includes the review of the Auditor General's Annual Report. The Committee holds public meetings and requires the Auditor General and other witnesses to appear and answer questions on matters raised in the Auditor General's Annual Report as well as other issues.

### **PROCEEDINGS AND RESULTS**

**13.3** The Committee held a number of meetings to review the observations and issues raised in my 2003 Annual Report. As of March 2, 2004, I appeared before the Committee on four occasions and assisted in their deliberations by providing further information, explanation and clarification on a number of issues raised in the Annual Report.

**13.4** Through its deliberations the Committee has an important role in contributing to improved accountability and effectiveness in government operations. I look forward to continuing to work with the Committee in fulfilling its mandate.



**OFFICE OF THE AUDITOR GENERAL**



# 14. OFFICE OF THE AUDITOR GENERAL

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## MANDATE AND MISSION

**14.1** The mandate of the Office is derived from the Audit Act. As a servant of the Legislative Assembly, the Auditor General is independent of government. Authority is given to carry out financial statement audits of the Public Accounts as well as any agency of government or Crown controlled or owned corporation.

**14.2** Under the Act, the Auditor General has a broad mandate to conduct any audit or examination he considers necessary to determine whether any agency of government is achieving its purposes and is doing so economically and efficiently in compliance with the applicable statutory requirements.

**14.3** The mission of the Office of the Auditor General is

- to conduct independent audits and examinations that provide objective information, advice, and assurance to the Legislative Assembly; and
- to promote best practices in government operations.

## RESPONSIBILITIES AND FUNCTIONS

**14.4** The Audit Act sets out the responsibilities of the Auditor General. The Auditor General is required to report annually on the results of the audits and examinations conducted by the Office. The work of the Office can be categorized into two main types of assignments - financial audits, and special audits and examinations.

**14.5** The primary responsibility of the Auditor General is the audit of the Public Accounts of the Province. The Auditor General is also named in legislation as the financial auditor for a number of Crown agencies.

**14.6** The mandate allows the Auditor General to conduct any audit or examination considered necessary to determine whether any agency of government is achieving its purpose, is doing so economically and efficiently and is complying with the applicable

## 14. Office of the Auditor General

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statutory provisions. Special examinations may include work on compliance with applicable authorities on a government-wide basis. In addition, the Act allows for special assignments or investigations at the request of the Lieutenant Governor in Council.

**14.7** The Office performs an important service to the Legislative Assembly. In some cases where government reports information about its performance, we comment on its completeness and accuracy and thus provide credibility and add value to that information. In other circumstances we audit government programs directly and report our findings to the Legislative Assembly and the public. The reports resulting from these assessments include recommendations and advice which can assist government in identifying opportunities for improvement in the management and control of public funds.

### OPERATING PHILOSOPHY

#### Independence

**14.8** The Auditor General is responsible to the Legislative Assembly, not government. The Office is positioned to offer impartial opinions and recommendations on government operations and management practices. The Audit Act establishes the legal framework for an independent audit office. The key components in building that independence include:

- the existence of a Legislative Audit Committee which reviews the Office's budget;
- the authority to carry out the audits and examinations which the Auditor General deems necessary;
- the right of access to records and information necessary to perform audit functions;
- the power to request and receive any information or explanations required; and
- the requirement to report annually to the Legislative Assembly.

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## 14. Office of the Auditor General

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**14.9** In addition, the independence of the Office is supported by an office code of conduct which includes, among other things, policy and guidance on integrity, impartiality, and potential conflict of interest situations.

### **Audit Planning**

**14.10** Each year an audit work plan is developed consistent with the audit priorities established by the Office and the resources available. The annual work plan includes a number of financial statement audits as well as special audits and examinations.

**14.11** Special audits and examinations of government departments and Crown agencies are carried out on a cyclical basis. These audits can vary in scope from the entire organization to a particular division or program. Audits are sometimes carried out on a particular function on a government-wide basis.

**14.12** Various factors are considered in establishing priorities for special audits and examinations. These include; materiality of revenues/expenditures, results of previous audits, the date of the last audit, and the impact on the public. Other factors considered in planning each audit include; our audit mandate, expected resources required to complete the audit, the quality of the financial and management controls in place for the entity, complexity of the operations, and possible matters of significance that may arise from the audit.

**14.13** Occasionally the Office is requested by Executive Council or the Legislative Assembly to carry out an examination or review for a particular purpose.

### **Professional Standards**

**14.14** Generally accepted accounting principles for government are established through the recommendations of the Public Sector Accounting Board of the Canadian Institute of Chartered Accountants (CICA). These recommendations are directed at the public sector and deal with numerous accounting issues. We rely on generally accepted

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## 14. Office of the Auditor General

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accounting principles for the public sector in conducting our audits as well as other guidance provided by the CICA.

**14.15** Our audits are conducted in accordance with generally accepted auditing standards. These standards relate to the professional qualifications of auditors, minimum examination requirements, and reporting responsibilities. They are designed to ensure that our audits are properly planned, conducted, and reported and that audit findings are based on well substantiated evidence.

**14.16** The Office is subject to a periodic practice inspection carried out by the Institute of Chartered Accountants of Prince Edward Island. This process is designed to protect the public interest by ensuring the Office meets the standards required of the profession.

### PERSONNEL, ADMINISTRATION AND AFFILIATIONS

#### Organization

**14.17** The Office staff complement consists of two audit directors, eleven auditors and two administrative staff. Four other auditor positions remain vacant due to lack of budgetary resources. With our limited staff we strive to provide audit coverage of significant areas of government on a cyclical basis.

**14.18** Under the Audit Act, the Legislative Audit Committee, a standing Committee of the Legislative Assembly, is responsible for the administration of the Office of the Auditor General. The Committee consists of the Speaker of the Legislative Assembly, who is Chairperson; the Leader of the Opposition; and the Provincial Treasurer. On an annual basis, the Committee reviews the budget estimates of the Office.

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## 14. Office of the Auditor General

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**14.19** For the year ended March 31, 2004 budgeted expenditures for the Office amounted to \$1,271,300 as follows.

	<b>2003-04 Budget Estimate</b>
Administration	\$ 28,000
Equipment	8,500
Materials, Supplies, and Services	10,200
Professional and Contract Services	32,500
Salaries	1,146,500
Travel and Training	33,000
Contribution - CCAF	12,600
Total	<u>\$1,271,300</u>

### **Professional Affiliations**

**14.20** As an Office we strive to keep current in all aspects of legislative and other audit practices, as well as new developments within the profession. The Office maintains a close association with a number of professional organizations, and experience and methodology is shared with a view to contributing to the continuing development of legislative audit practices. Some of the key affiliations include the following:

- The Canadian Council of Legislative Auditors (CCOLA) - The meetings of the Council bring together legislative auditors from the federal government and the provinces and provides an opportunity for information exchange, discussion, and development and enhancement of legislative audit practices. Members of the Office serve on various CCOLA committees.
- The Public Sector Accounting Board - The Office provides input and cooperates with the Board in its efforts to improve and harmonize public sector accounting practices across Canada. The Board conducts research and issues recommendations on public sector accounting issues.
- The Canadian Institute of Chartered Accountants and the Institute of Chartered Accountants of Prince Edward Island - The Office maintains an important professional relationship with these

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## 14. Office of the Auditor General

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organizations and provides input and receives information on developments in the profession through membership on various committees.

- The CCAF - The Office has been a member and supporter of the CCAF since its inception in 1980. CCAF is a Canadian research and education foundation dedicated to building knowledge for meaningful accountability and effective governance, management, and audit. During the last year CCAF issued a document; Reporting Principles: Taking Public Performance Reporting to a New Level. The document's goal is to help government advance the quality of their reporting on performance.

### OBJECTIVES AND ACCOMPLISHMENTS

**14.21** In accordance with its mandate, the Office has established two broad goals:

- (I) To promote improved accountability for, and management of, public funds.*
- (II) To continuously update our knowledge and skills within our field of practice and to work to the highest standard of our profession.*

In support of these goals, the Office has developed a number of objectives. The following paragraphs provide information on each of these objectives and the accomplishments during the year.

- (i) To prepare an Annual Report for the Legislative Assembly, as required under the Audit Act, on the results of the audits that have been carried out.**

**14.22** The Annual Report provides information on significant issues and recommendations resulting from our work. We expect that the Annual Report presented each year will act as a vehicle for positive change in the management and performance of the public sector. The deliberations and discussions on the Report that occur within the

## 14. Office of the Auditor General

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Legislative Assembly and by the Standing Committee on Public Accounts provide the impetus to bring about the improvements recommended in the Report.

**14.23** The 2003 Annual Report of the Auditor General was tabled in the Legislative Assembly on April 8, 2003. The Report was referred to the Public Accounts Committee and a number of meetings were held to discuss the Annual Report and provide additional information and explanations to the Committee.

**(ii) To express opinions on the financial statements of the Public Accounts of the Province and other Crown agencies subject to audit.**

**14.24** An unqualified opinion was provided on the Public Accounts for the year ended March 31, 2003. We continue to work closely with the Office of the Comptroller in improving the financial statement presentation and disclosure. In addition to the Public Accounts, we conduct a number of financial statement audits of Crown Corporations, Pension and Trust Funds, and other Agencies. This process provides assurance to the taxpayers, through the Legislative Assembly, on the fairness of information reported by government.

**(iii) To perform selective special audits and examinations to determine whether departments and agencies are being managed with due regard for economy and efficiency and are in compliance with applicable statutory provisions.**

**14.25** The Office has a limited amount of resources to carry out its work. Many of the financial statement audits which we perform are required under legislation. The extent of special audit and examination work that we can undertake is determined by the resources available after the financial audit work has been assigned.

**14.26** Our special audits and examinations provide information and assurance on the management of public resources in a number of areas. We provide advice and make recommendations to improve management controls and practices where problems are identified.

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## 14. Office of the Auditor General

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- (iv) To perform other investigations as may be required from time to time.**

**14.27** Occasionally we are asked to investigate potential weaknesses in control or to follow up on specific observations from our reports.

**14.28** It has been our practice to follow up on outstanding recommendations and provide information in our Annual Report on the status of implementation of the recommendations arising from our audits. This is part of the legislative audit function which provides important feedback to the Public Accounts Committee, and assists in its role of holding government accountable.

- (v) To maintain technical competence in an evolving accounting and auditing environment.**

- (vii) To remain aware of and provide input to the development of public sector accounting standards.**

- (viii) To build leadership within the Office by providing professional development and training opportunities for staff.**

**14.29** Our Office maintains an affiliation with the Canadian Institute of Chartered Accountants which helps us to keep up to date on emerging accounting and auditing issues. Standards are promulgated by the Public Sector Accounting Board and the Assurance Standards Board. We regularly participate in this process by providing comments during the discussion stages of the development of government accounting standards. In addition we maintain professional affiliations with the Canadian Council of Legislative Auditors and the CCAF. This participation allows us to share knowledge and experience as well as receive information on newly developed methodology.

**14.30** Audit staff within the Office have professional accounting designations. We strive to provide training and professional development opportunities to staff. Individual staff members attend various professional conferences, seminars and meetings.

# SCHEDULES



**OPERATING FUND  
APPROPRIATIONS**

<u>ORDINARY</u>	<u>ORIGINAL APPROPRIATION ACT 2002/2003</u>	<u>TRANSFERS</u>	<u>SPECIAL WARRANTS</u>	<u>TOTAL BUDGET</u>	<u>APPROPRIATION ACT EXPENDITURES 2002/2003</u>	<u>PUBLIC ACCOUNTS EXPENDITURES 2002/2003</u>
AGRICULTURE AND FORESTRY	\$ 30,248,400	\$ -	\$ 588,000	\$ 30,836,400	\$ 29,420,844 <b>Note 1</b>	\$ 29,156,558
PEI GRAIN ELEVATORS CORPORATION	165,000	-	-	165,000	165,000	165,000
OFFICE OF THE ATTORNEY GENERAL	29,739,800	-	998,600	30,738,400	30,720,421	30,720,421
AUDITOR GENERAL	1,229,600	-	-	1,229,600	1,018,547	1,018,547
COMMUNITY AND CULTURAL AFFAIRS	20,104,100	-	63,000	20,167,100	19,816,082	19,816,082
DEVELOPMENT AND TECHNOLOGY	6,267,900	-	23,600	6,291,500	6,181,252	6,181,252
TECHNOLOGY ASSET MANAGEMENT	1,876,400	-	-	1,876,400	1,849,995	1,849,995
PEI BUSINESS DEVELOPMENT INC.	30,022,000	-	3,092,000	33,114,000	33,107,000	33,107,000
EMPLOYMENT DEVELOPMENT AGENCY	3,288,900	-	1,500,000	4,788,900	4,708,529	4,708,529
PEI ENERGY CORPORATION	723,400	-	-	723,400	671,300	671,300
EDUCATION	201,923,700	542,800	4,937,000	207,403,500	207,380,031 <b>Note 2</b>	199,189,212
ISLAND REGULATORY AND APPEALS COMMISSION	1,065,100	-	-	1,065,100	1,065,000	1,065,000
EXECUTIVE COUNCIL	3,180,300	48,200	105,000	3,333,500	2,951,471	2,951,471
FISHERIES, AQUACULTURE AND ENVIRONMENT	8,255,300	-	-	8,255,300	8,161,895 <b>Note 1</b>	8,426,181
HEALTH AND SOCIAL SERVICES	389,174,200	4,236,200	259,600	393,670,000	392,708,278 <b>Note 2</b>	392,492,798
EAST PRINCE HEALTH FACILITY	21,000,000	-	-	21,000,000	17,451,327	17,451,327
LEGISLATIVE ASSEMBLY	3,101,800	-	30,000	3,131,800	3,118,730	3,118,730
PROVINCIAL TREASURY	18,778,500	-	62,700	18,841,200	18,229,280	18,229,280

See notes on page 3

**OPERATING FUND  
APPROPRIATIONS**

<u>ORDINARY</u>	<u>ORIGINAL APPROPRIATION ACT 2002/2003</u>	<u>TRANSFERS</u>	<u>SPECIAL WARRANTS</u>	<u>TOTAL BUDGET</u>	<u>APPROPRIATION ACT EXPENDITURES 2002/2003</u>	<u>PUBLIC ACCOUNTS EXPENDITURES 2002/2003</u>
GENERAL GOVERNMENT	\$ 8,074,600	\$(4,827,200)	\$ 7,879,000	\$ 11,126,400	\$ 11,081,338	\$ 11,081,338
PEI LENDING AGENCY	790,700	-	-	790,700	790,261	790,261
COUNCIL OF MARITIME PREMIERS	183,700	-	-	183,700	183,078	183,078
INTERMINISTERIAL WOMEN'S SECRETARIAT	299,700	-	-	299,700	285,869	285,869
PEI PUBLIC SERVICE COMMISSION	6,395,800	-	21,100	6,416,900	5,228,432	5,228,432
EMPLOYEE BENEFITS	11,344,200	-	6,953,926	18,298,126	18,298,125	Note 2 707,588
TOURISM	108,900	-	-	108,900	101,485	101,485
TOURISM PEI	11,333,100	-	-	11,333,100	11,163,549	11,163,549
TRANSPORTATION AND PUBLIC WORKS	69,430,300	-	-	69,430,300	67,713,629	67,713,629
INTEREST CHARGES ON DEBT	106,500,000	-	-	106,500,000	100,934,520	100,934,520
PENSION AND RETIREMENT BENEFITS	-	-	-	-	-	Note 2 25,996,836
<b>TOTAL ORDINARY</b>	<b>\$ 984,605,400</b>	<b>\$ -</b>	<b>\$26,513,526</b>	<b>\$ 1,011,118,926</b>	<b>\$ 994,505,268</b>	<b>\$ 994,505,268</b>
<u><b>CAPITAL</b></u>						
TRANSPORTATION AND PUBLIC WORKS	16,381,000	-	8,019,000	24,400,000	24,269,865	24,269,865
<b>GRAND TOTAL</b>	<b><u>\$1,000,986,400</u></b>	<b><u>\$ -</u></b>	<b><u>\$34,532,526</u></b>	<b><u>\$1,035,518,926</u></b>	<b><u>\$1,018,775,133</u></b>	<b><u>\$1,018,775,133</u></b>

See notes on page 3

OPERATING FUND  
APPROPRIATIONS

**Note 1:** For presentation purposes, the Public Accounts were adjusted to reflect the transfer of the Pesticide Regulatory Program from Agriculture and Forestry to Fisheries, Aquaculture and Environment.

	<u>Per Appropriation Act</u>	<u>Transfer of Pesticide Regulatory Program</u>	<u>Per Public Accounts</u>
Agriculture and Forestry	\$29,420,844	\$(264,286)	\$29,156,558
Fisheries, Aquaculture and Environment	\$8,161,895	\$264,286	\$8,426,181

**Note 2:** Appropriations and expenditures are presented in accordance with the classifications in the Appropriation Act 2002. During the year, expenditures were recorded on the same basis as the Appropriation Act 2002. This differs from the format used in the Public Accounts in which expenditures (Pension and Retirement Benefits) were reclassified at year end.

	<u>Per Appropriation Act</u>			
	<u>Regular</u>	<u>Pension and Retirement Benefits</u>	<u>Total</u>	<u>Per Public Accounts</u>
Education	\$199,189,212	\$ 8,190,819	\$207,380,031	\$199,189,212
Health and Social Services	392,492,798	215,480	392,708,278	392,492,798
Employee Benefits	707,588	17,590,537	18,298,125	707,588
Pension and Retirement Benefits	-	-	-	25,996,836
	<u>\$592,389,598</u>	<u>\$25,996,836</u>	<u>\$618,386,434</u>	<u>\$618,386,434</u>



**ORDER-IN-COUNCIL**

**LIST OF SPECIAL WARRANTS**

**AGRICULTURE AND FORESTRY**

EC 2002-559 INDUSTRY DEVELOPMENT

AERC Program \$ 588,000

To fund projects under the Sustainable Resource Conservation Program. The expenditure was to be offset 100 percent by revenue from the Special Projects Sustainable Resource Support Fund.

**OFFICE OF THE ATTORNEY GENERAL**

EC 2002-616 LEGAL AND JUDICIAL SERVICES

Salaries \$ 22,600

**ACCESS AND PRIVACY SERVICES**

Administration	21,800	
Materials, supplies and services	10,600	
Professional and contract services	2,500	
Salaries	56,200	
Travel	<u>20,600</u>	\$ 134,300

To fund the establishment of an Access and Privacy Services Office. The expenditure was to be offset 100 percent by the sequestration of funds originally budgeted in Executive Council.

EC 2003-126 ADMINISTRATION

Materials, supplies and services \$ 21,000

**LEGAL AND JUDICIAL SERVICES**

Materials, supplies and services	55,000	
Salaries	27,500	
Professional and contract services	536,300	

**CROWN ATTORNEY**

Materials, supplies and services 56,000      695,800

To fund costs related to RCMP contracts, and other expenditures in the Office of the Attorney General.

**ORDER-IN-COUNCIL**

**LIST OF SPECIAL WARRANTS**

EC 2004-92	LEGAL AND JUDICIAL SERVICES		
	Professional and contract services	\$ 79,000	
	COMMUNITY AND CORRECTIONAL SERVICES		
	Salaries	80,100	
	JUSTICE POLICY		
	Grants - Human Rights Commission	<u>9,400</u>	<u>\$ 168,500</u>
	<p>To provide funding for excess expenditures in the Office of the Attorney General for the 2002/2003 fiscal year. The expenditure was to be partially offset by \$100,000 in federal revenue.</p>		
	Total		<u>\$ 998,600</u>

**COMMUNITY AND CULTURAL AFFAIRS**

EC 2002-617	CULTURE, HERITAGE, RECREATION AND SPORTS		
	Salaries		<u>\$ 63,000</u>
	<p>To reassign an employee of the Freedom of Information and Protection of Privacy Implementation Team from Executive Council. The expenditure was to be offset 100 percent by the sequestration of funds originally budgeted in Executive Council.</p>		

**DEVELOPMENT AND TECHNOLOGY**

EC 2002-618	DEPARTMENTAL MANAGEMENT		
	Salaries		<u>\$ 23,600</u>
	<p>To reassign two employees of the Freedom of Information and Protection of Privacy Implementation Team from Executive Council. The expenditure was to be offset 100 percent by the sequestration of funds originally budgeted in Executive Council.</p>		

**ORDER-IN-COUNCIL**

**LIST OF SPECIAL WARRANTS**

**PEI BUSINESS DEVELOPMENT INC.**

EC 2003-69	Infrastructure assistance Technology PEI Inc.	\$2,100,000 <u>992,000</u>	<u>\$3,092,000</u>
	To fund additional infrastructure program activities and projected losses for the Atlantic Technology Centre.		

**EMPLOYMENT DEVELOPMENT AGENCY**

EC 2002-303	JOB CREATION AND PLACEMENT		
	Grants		<u>\$1,500,000</u>
	To provide funding to meet demands for job creation project placements.		

**EDUCATION**

EC 2003-127	CORPORATE SERVICES AND SCHOOL BOARD OPERATIONS		
	Salaries	\$ 837,000	
	School construction and capital repair	<u>1,330,000</u>	\$2,167,000
	To fund Kinkora High School construction costs and provide additional funding to school boards.		

EC 2003-158	CONTINUING EDUCATION AND TRAINING		
	Grants		<u>2,770,000</u>
	To fund obligations contained in the Skills Development Contribution Agreement. The expenditure was to be offset 100 percent by federal revenue.		

	Total		<u>\$4,937,000</u>
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**EXECUTIVE COUNCIL**

EC 2003-70	INTERGOVERNMENTAL AFFAIRS		
	Professional and contract services	\$ 30,000	
	Grants	<u>75,000</u>	<u>\$ 105,000</u>
	To fund community initiatives and translation services associated with the French Language Services Act. The expenditure was to be offset 100 percent by federal revenue.		

**ORDER-IN-  
COUNCIL**

**LIST OF SPECIAL WARRANTS**

**HEALTH AND SOCIAL SERVICES**

EC 2003-41 DEPARTMENT MANAGEMENT SERVICES  
PUBLIC HEALTH AND EVALUATION SERVICE

Health Research Program \$ 259,600

To fund projects of the Health Research Fund. The expenditure was to be offset 100 percent by revenue from the Special Projects Health Research Fund.

**LEGISLATIVE ASSEMBLY**

EC 2002-619 OFFICE OF THE INFORMATION AND PRIVACY COMMISSIONER

Professional and contract services \$ 30,000

To fund the Office of the Information and Privacy Commissioner. The expenditure was to be offset 100 percent by the sequestration of funds originally budgeted in Executive Council.

**PROVINCIAL TREASURY**

EC 2003-159 INFORMATION TECHNOLOGY MANAGEMENT GROUP

Equipment \$ 62,700

To fund the cost of computer software upgrades throughout Government. The expenditure was to be offset 100 percent by revenue from Government Departments.

**GENERAL GOVERNMENT**

EC 2003-128 SALARY NEGOTIATIONS

Salaries \$1,879,000

To fund additional forecast expenditures for negotiated union agreements.

EC 2004-94 Provision for guaranteed debt 6,000,000

To establish a provision for losses on debt guaranteed by the Province.

Total \$7,879,000

**ORDER-IN-  
COUNCIL**

**LIST OF SPECIAL WARRANTS**

**PEI PUBLIC SERVICE COMMISSION**

EC 2002-506 LEARNING AND STAFF DEVELOPMENT

Administration	\$	1,000	
Materials, supplies and services		1,000	
Salaries		<u>19,100</u>	<u>\$ 21,100</u>

To fund the implementation of the French Language Services Act. The expenditure was to be offset 100 percent by federal revenue under the Canada/ Prince Edward Island General Agreement on the Promotion of Official Languages.

**EMPLOYEE BENEFITS**

EC 2004-93 EMPLOYEES FUTURE BENEFITS

Interest on funded and unfunded pensions and benefits			<u>\$6,953,926</u>
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To cover expenses incurred to comply with Public Sector Accounting Recommendations.

**TRANSPORTATION AND PUBLIC WORKS - CAPITAL**

EC 2003-42 CAPITAL EXPENDITURE - HIGHWAYS

Bridges and culverts	\$	475,000	
Paving		1,780,700	
Highway reconstruction		3,825,300	
Strategic Highway Infrastructure Program		1,330,000	

**CAPITAL EXPENDITURE - BUILDINGS**

Prince County Courthouse		<u>608,000</u>	<u>\$8,019,000</u>
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To fund capital expenditures for highway improvements and renovations to the Prince County Courthouse. The expenditures for highway improvements were to be partially offset by \$2,374,000 in federal revenue from Transport Canada and from the Disaster Financial Assistance Agreement.