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Chapter 1
Introductory Comments

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Introductory Comments

Volume I Reports Our Financial Audit Work

1.1 This volume of our Report deals with matters arising from our financial audits of the Province and its Crown agencies for the year ended March 31, 2014.

Release of 2014 Province of New Brunswick financial statements – earliest release date in years

1.2 On July 17, 2014 I signed an unqualified audit opinion on the 2014 consolidated financial statements of the Province of New Brunswick. The government released the audited financial statements on July 23, 2014. This was the earliest release date in many years. Financial information is most useful if it is timely.

1.3 The early release date was in response to the *Fiscal Transparency and Accountability Act* which required the Auditor General to express her opinion as to whether the information is fairly presented at least 60 days before the date of the scheduled general election. The election was held on September 22, 2014.

Auditor General prefers earlier release of audited financial statements every year

1.4 I would like to make note of the significant collective effort of many participants throughout government departments, Crown corporations and agencies and especially the Office of the Comptroller. All of these participants worked diligently with my staff to achieve this milestone.

1.5 I am hopeful earlier financial statement release dates will become routine each and every year, not just when there is a provincial election.

Auditor General's Comments on the Province's Fiscal Status

1.6 The Province's fiscal situation remains a concern. The Province's March 31, 2014 audited consolidated financial statements show a sixth consecutive deficit of nearly half a billion dollars. A similar amount was added to Net Debt. Net Debt is now over $11.6 billion or $15,400 per New Brunswicker. The continued increase in Net Debt represents a very disturbing trend.

1.7 As I have stated in prior years this is not sustainable.

1.8 However, I would like to highlight once again recent government efforts to control spending. Our analysis shows New Brunswick's average three year expense growth rate was actually a decrease (from 2012 to 2014) of less than 1%. This was largely due to curtailing growth in the two largest expenditure areas of Health and Education and Training.

1.9 Although recent government efforts to control spending are noteworthy, it is not enough. Particularly given revenues are not keeping pace and show minor growth of only 1.4% (three year average growth rate).

1.10 The Province's structural deficit continues. A structural deficit is a sustained situation where expenses exceed revenues. It is also concerning that this fiscal imbalance persists in a time when our infrastructure such as buildings, roads and bridges are not being maintained and renewed at optimal levels. In general, to correct a structural deficit, expenses or services/programs need to be reduced, revenues need to be increased, or some combination of the two need to occur. The solution chosen is dependent on government policy and decision making.

Continued diligence is needed to improve the financial health of the Province

1.11 Continued fiscal diligence is required in government policy and decision making to improve the financial health of the Province.

Need to return to balanced budgets and control growth in Net Debt

1.12 Our Province must return to balanced budgets in the foreseeable future. As well, our Province must control Net Debt growth. Both measures, the annual deficit and change in Net Debt, are important in assessing the financial health of the Province.

1.13 Chapter 2 of this volume provides further detail, analysis and commentary of the Province's fiscal status as at March 31, 2014. The chapter includes historical trends, financial indicators and an analysis of New Brunswick's Net Debt compared to that of other provinces. Our analysis shows when compared to other provinces, New Brunswick's Net Debt has increased the most over the last eight years. This is cause for concern for the long term sustainability of the Province.

Observations on Pension Plans

1.14 Significant changes have been made to some of the Province's pension plans in the past two years. In particular the largest public service plan was converted during fiscal 2014 to a Shared Risk Pension Plan. This followed the conversion of two smaller plans in 2013. Given these significant changes, Chapter 3 presents observations and comments on complex issues regarding pensions.

1.15 For the year ended 31 March 2014 pension expense of $365.4 million was recorded. The 2014 elimination of special payments to pension plans resulted in an estimated annual cash flow savings of over $150 million. These cash savings will compound over time.

1.16 Chapter 3 also discusses the funding status of the public service pension plan both before and after conversion to a shared risk pension structure. We also illustrate the significance of the impact on employees of the former PSSA plan changes.

1.17 As a result of plan changes, employees will pay more in contributions; receive lower benefits, work longer or a combination of all three of these outcomes. In particular the pension plan changes will impact new and middle career employees the most, with employees near retirement being less affected by plan changes.

Other Chapters in this Volume

1.18 Chapter 4 reports on matters arising from our audit of the financial statements of the Province.

1.19 Chapter 5 reports on matters arising from our audits of Crown agencies and Federal Claims.

Acknowledgements

1.20 My Office is grateful for the continuing cooperation we receive from government departments and agencies during the course of our financial audit work.

1.21 I want to thank all staff of my Office for their hard work and dedication. It is a small group of professionals committed to fulfilling the mandate of the Office and producing a quality report to the Legislative Assembly. The report we are presenting today is a reflection of a team effort where each member of the staff has greatly contributed.

Kim MacPherson, CPA,CA
Auditor General

Chapter 2
Comments on the Province's Financial Position

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Comments on the Province's Financial Position

Sixth Consecutive Deficit

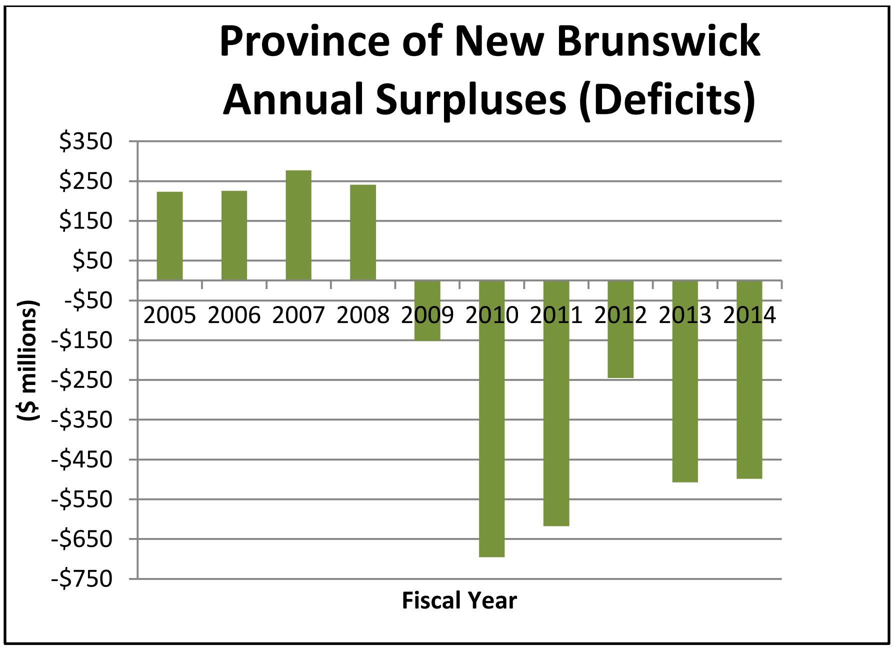
2.1 The Province's 31 March 2014 audited consolidated financial statements reported a deficit of $498.7 million and an increase in Net Debt for the fiscal year of $510.6 million. The Province now has a Net Debt of $11.6 billion.

2.2 The $498.7 million annual deficit was higher than the budgeted deficit of $478.7 million and was lower than the prior year deficit of $507.5 million.

Action is Required

2.3 This represents the sixth consecutive annual deficit. To assist in financing these deficits, the Province has incurred additional debt. This trend is very concerning. Significant changes are required to improve the financial health of the Province.

Exhibit 2.1 - Annual Surpluses (Deficits)



As restated

Exhibit 2.2 - Annual Surpluses (Deficits) Data

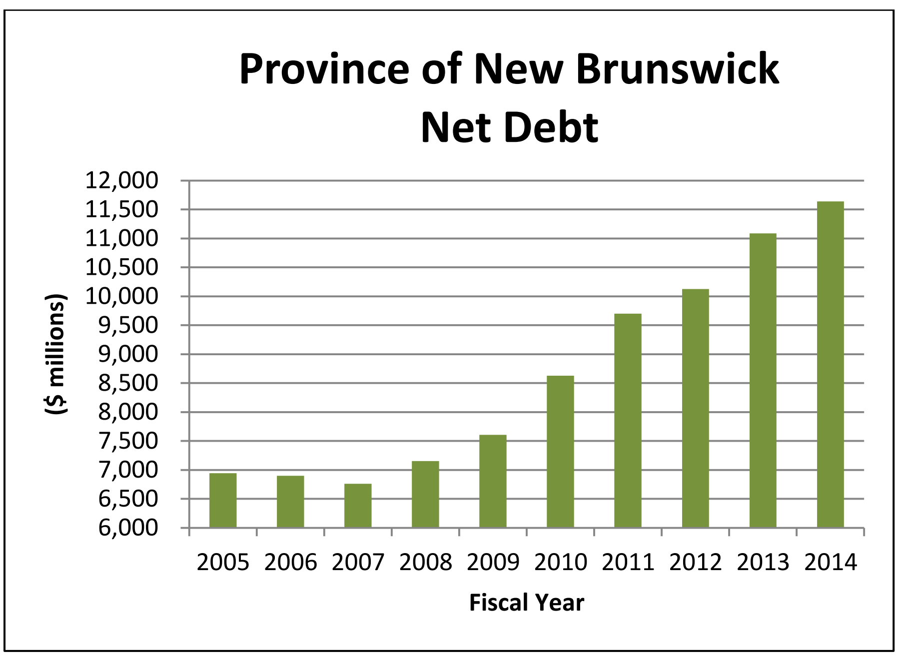
Annual Surpluses (Deficits) ($ millions)										
	2005	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**
As restated	223.2	225.3	277.3	241.1	(152.0)	(695.9)	(617.2)	(244.8)	(507.5)	n/a
As originally recorded	242.2	243.6	236.8	86.7	(192.3)	(737.9)	(633.0)	(260.6)	(507.7)	(498.7)

2.4 Exhibits 2.1 and 2.2 show the surplus or deficit for the past ten years. The preceding years' amounts have been restated as per Note 18 of the Province's 31 March 2014 consolidated financial statements.

Continued Growth in Net Debt

2.5 Net Debt is one of the most important measures of the financial position of the Province. Exhibits 2.3 and 2.4 show Net Debt for the past ten years. Net Debt measures the difference between a government's liabilities and financial assets. This difference provides a measurement of the future revenues required to pay for past transactions and events.

Exhibit 2.3 - Province of New Brunswick Net Debt



As restated

Exhibit 2.4 - Net Debt Data

Net Debt ($ millions)										
	2005	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**
As restated	6,943.0	6,900.6	6,761.4	7,151.6	7,608.0	8,628.9	9,700.4	10,125.8	11,084.6	n/a
As originally recorded	6,836.0	6,655.7	6,577.9	6,942.9	7,387.8	8,353.0	9,480.4	10,045.8	11,054.0	11,641.2

2.6 We would like to draw attention to the following facts:

- For the year ended 31 March 2014, Net Debt increased by $510.6 million to $11.6 billion (net of a $46 million adjustment to opening net debt and accumulated deficit relating to the amalgamation of the New Brunswick Power Group of Companies, New Brunswick Electric Finance Corporation and the New Brunswick System Operator).
- In the eight years since 2006, Net Debt has increased $4.7 billion.
- The 2014-2015 Main Estimates budgets for an increase in Net Debt of $530.7 million for the year ended 31 March 2015.
- Based on 2014-2015 Main Estimates, Net Debt of the Province could be in excess of $12 billion for the year ended 31 March 2015.

New Brunswick's credit ratings

2.7 This continued increase in Net Debt represents a very disturbing trend. An even higher demand will exist on future revenue to pay past expenses. Such continued negative trends impacted the Standard & Poor's decision to downgrade the Province's credit rating from AA- to A+ in 2012. This downgrade results in more expensive borrowing costs and may constrain future borrowing capacity of the Province.

2.8 Exhibit 2.5 shows the Province's credit rating as determined by various credit rating agencies. All three ratings remained unchanged from previous years in 2014. The rating agencies noted stable trends, however showed concern by the deterioration in fiscal outlook and the budgeted higher deficit going forward. Even with stable ratings the Province's borrowing capacity may be negatively affected with New Brunswick's increased debt burden.

2.9 Exhibit 2.6 shows the most recent credit ratings for other provinces compared to New Brunswick. These provinces are consistently rated in the good credit quality range; however, according to Moody's Investors Services, "the continued accumulation of debt and difficulty in returning to balanced budgets is increasing negative credit pressure for some provinces" and therefore could negatively affect these ratings in the future.

Exhibit 2.5 - New Brunswick's Credit Ratings

Year	Dominion Bond Rating Services (DBRS)	Moody's Investors Services	Standard & Poor's
2014	A (high)	Aa2	A+
2013	A (high)	Aa2	A+
2012	A (high)	Aa2	A+
2011	A (high)	Aa2	AA-
2010	A (high)	Aa2	AA-

Exhibit 2.6 - Credit Ratings of Other Provinces

Province	Dominion Bond Rating Services (DBRS)	Moody's Investors Services	Standard & Poor's
Saskatchewan	AA	Aaa	AAA
Manitoba	A (high)	Aa1	AA
Nova Scotia	A (high)	Aa2	A+
New Brunswick	A (high)	Aa2	A+
Newfoundland and Labrador	A	Aa2	A+

Balanced budget commitment

2.10 The new *Fiscal Transparency and Accountability Act* includes objectives to balance the budget, decrease Net Debt and Net Debt to GDP ratio and provide quarterly financial updates.

2.11 Noted in both the *Fiscal Transparency and Accountability Act* and the 2014-2015 budget speech is a multi-year fiscal plan which outlines a target to return to a balanced budget by 2017-2018. Given the September 2014 change in government it is uncertain whether this legislation will remain in force. The recently elected Liberal Government indicated in its election platform a return to a balanced budget within six years. We are hopeful the commitment to returning to a balanced budget state in the near term will continue. However, the achievement of these goals will require increased fiscal diligence.

2.12 The *Fiscal Transparency and Accountability Act* expects the Net Debt to GDP ratio will be at or below 35% by March 2019. For the fiscal year ended 31 March 2014 New Brunswick's Net Debt as a percentage of GDP was 36.7% (Exhibit 2.14). The Province will need to increase efforts to meet this requirement.

Net Debt growth through budget deficits

2.13 Exhibit 2.7 shows the annual budgeted surplus/deficit for the Province for the last five years. Even though expenditure growth is slowing, budgeted deficits have been planned in the last five years which have contributed to Net Debt growth. In order to reduce Net Debt, the budgeted surplus/deficit needs improvement (i.e. through either increases to revenues, reductions to expenses, or a combination of both). If no other plan of action is taken, the deficit and Net Debt increases will continue.

Exhibit 2.7 - Annual Budgeted Surplus/Deficit.

Annual Budgeted Surplus/(Deficit) ($ millions)					
	2010	**2011**	**2012**	**2013**	**2014**
Budgeted Surplus/(Deficit)	(740.9)	(748.8)	(448.8)	(182.9)	(478.7)

Comparison to Other Provinces

2.14 Another way to assess the significance of the size of the Province's Net Debt is to compare it to the Net Debt of other provinces in absolute amount, per capita and as a percentage of GDP. Provinces used in our comparison include Newfoundland and Labrador, Nova Scotia, Manitoba and Saskatchewan. These provinces presented for comparison purposes were selected based on application of judgement where similarities in population and economic circumstances were considered. The provinces' application of accounting principles may differ upon comparing financial information, depending on particular circumstances. Population data for provinces used in our comparison is found in Exhibits 2.8 and 2.9.

2.15 In the next eight exhibits:

- information from the audited summary financial statements of the individual provinces is used;
- information about population is taken from the Statistics Canada website, and
- GDP figures are from the financial statement discussion and analysis attached to the individual provinces' audited summary financial statements.

Exhibit 2.8 - Provincial Population as of July 1, 2013

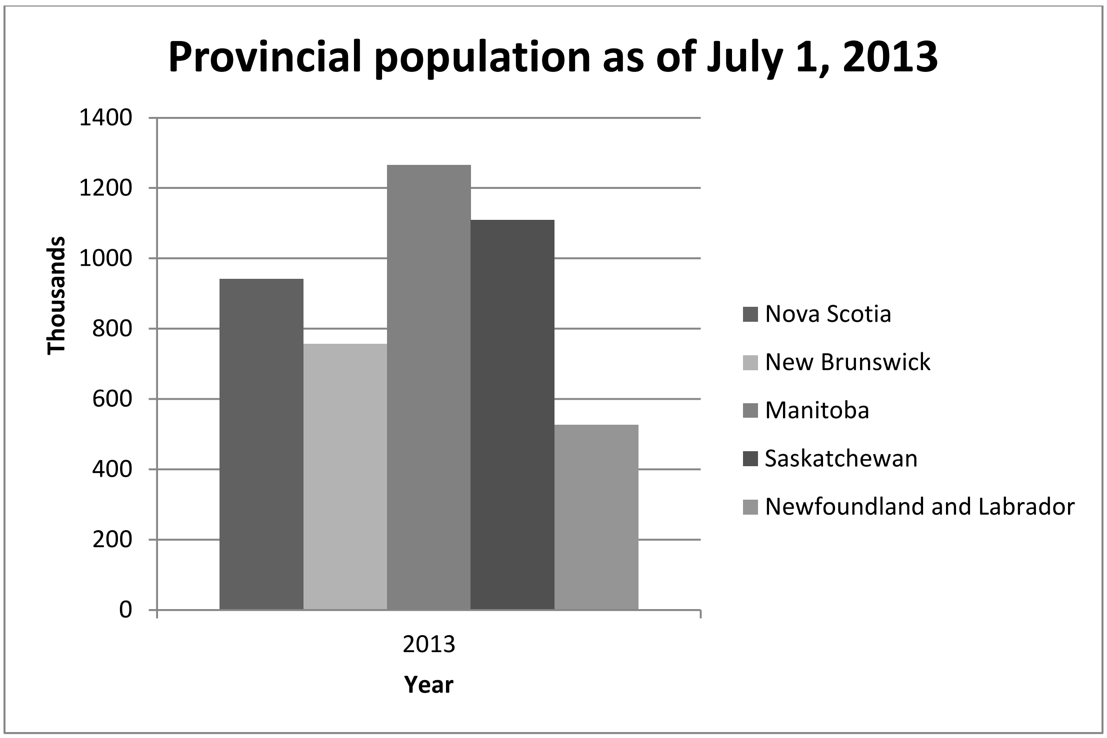


Exhibit 2.9 - Provincial Population as of July 1 Data

Provincial Population Data as of July 1			
Province	**(thousands)**		
	2009	**2012**	**2013**
Nova Scotia	938.2	945.1	940.8
New Brunswick	750.0	757.0	756.1
Manitoba	1,208.6	1,250.0	1,265.0
Saskatchewan	1,034.8	1,087.5	1,108.3
Newfoundland and Labrador	516.7	526.8	526.7

Exhibit 2.10 - Net Debt Comparison to Other Provinces

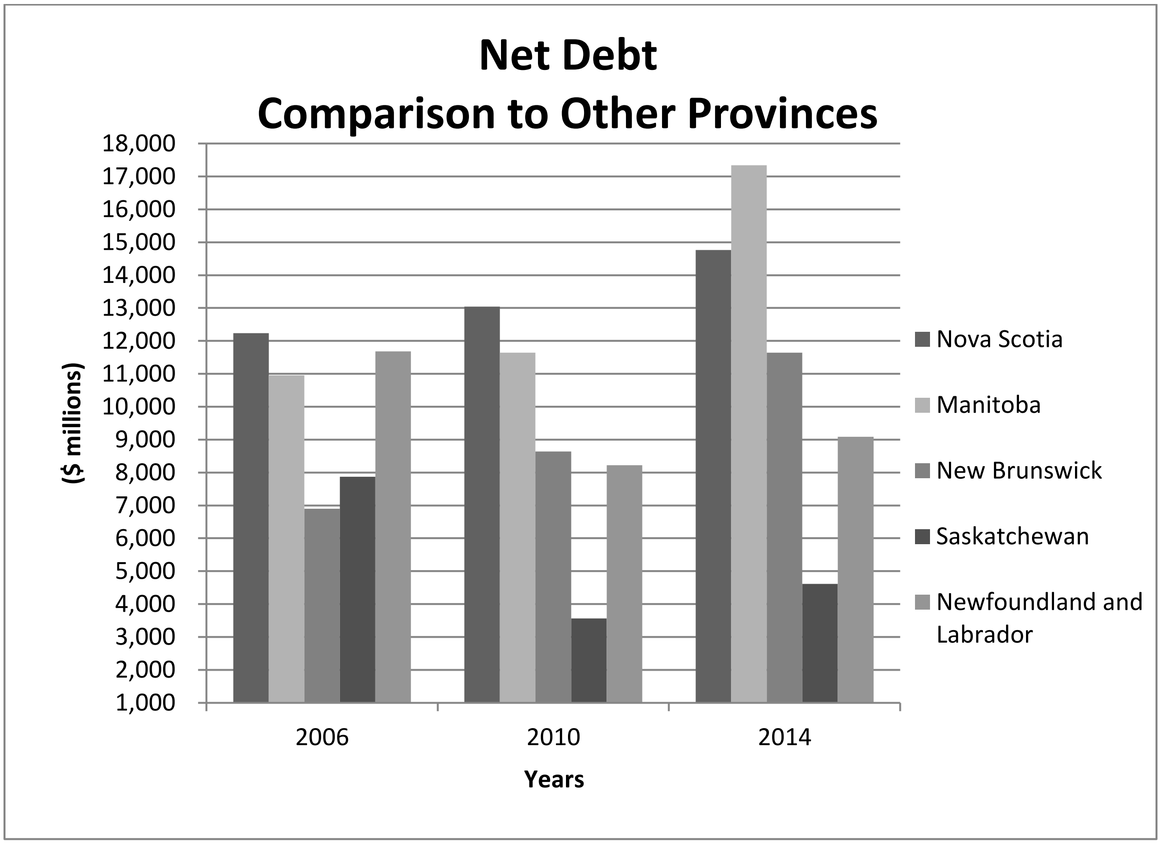


Exhibit 2.11 - Net Debt Comparison to Other Provinces Data

Net Debt Comparison to Other Provinces ($ millions)				
Province	**Increase (Decrease) 2006 to 2014**	**2006**	**2010**	**2014**
New Brunswick	69%	6,901	8,629	11,641
Saskatchewan	(41%)	7,870	3,560	4,615
Manitoba	58%	10,952	11,643	17,344
Nova Scotia	21%	12,239	13,045	14,762
Newfoundland and Labrador	(22%)	11,680	8,220	9,085

2.16 Exhibits 2.10 and 2.11 show that over the last eight years within this group, New Brunswick has had the highest increase in Net Debt. New Brunswick's rate of Net Debt growth has increased by 69% over the last eight years. The magnitude of this increase is very concerning. The overall debt burden for the Province remains at an elevated level. The 2014-2015 Main Estimates budgets an increase in Net Debt of approximately $530.7 million. The continued increase in Net Debt causes concern for the long term sustainability of the Province.

Exhibit 2.12 - Net Debt Per Capita Comparison to Other Provinces

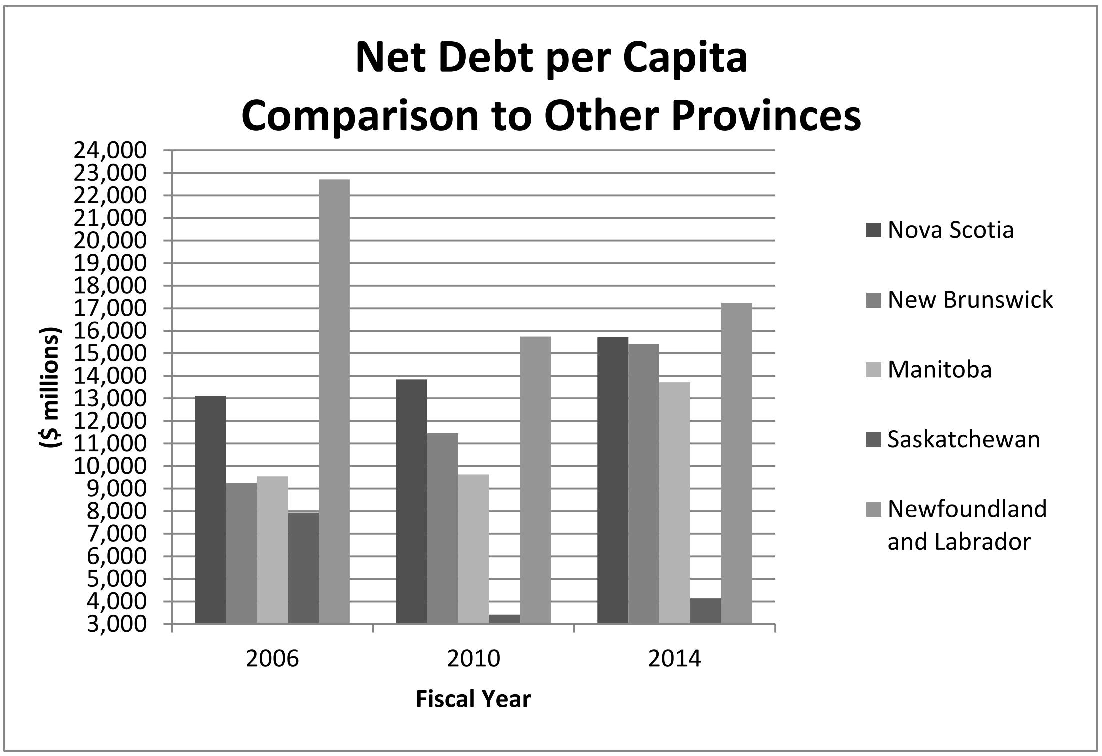


Exhibit 2.13 - Net Debt Per Capita Comparison to Other Provinces Data

Net Debt Per Capita Comparison to Other Provinces* ($)			
Province	**2006**	**2010**	**2014**
Nova Scotia	13,104	13,847	15,712
New Brunswick	9,255	11,459	15,400
Manitoba	9,537	9,633	13,711
Saskatchewan	7,940	3,410	4,130
Newfoundland and Labrador	22,716	15,748	17,240

**Amounts from provinces' 2014 financial statement discussion and analysis where available. For those provinces where this indicator was not published in the same format, information was obtained on population from Statistics Canada as of July 1 within the fiscal year. (i.e. 2014 was July 1 2013 population). Numbers have been rounded for presentation purposes.*

2.17 Information in Exhibits 2.12 and 2.13 show that New Brunswick has the third highest Net Debt per capita in the comparable group. If the debt were to be eliminated by way of contributions from New Brunswickers, each would contribute $15,400. Again, this indicator has increased significantly from 2010 at $11,459 to 2014 at $15,400 (a 34.4% increase in four years).

Exhibit 2.14 - Net Debt as a Percentage of GDP Compared to Other Provinces

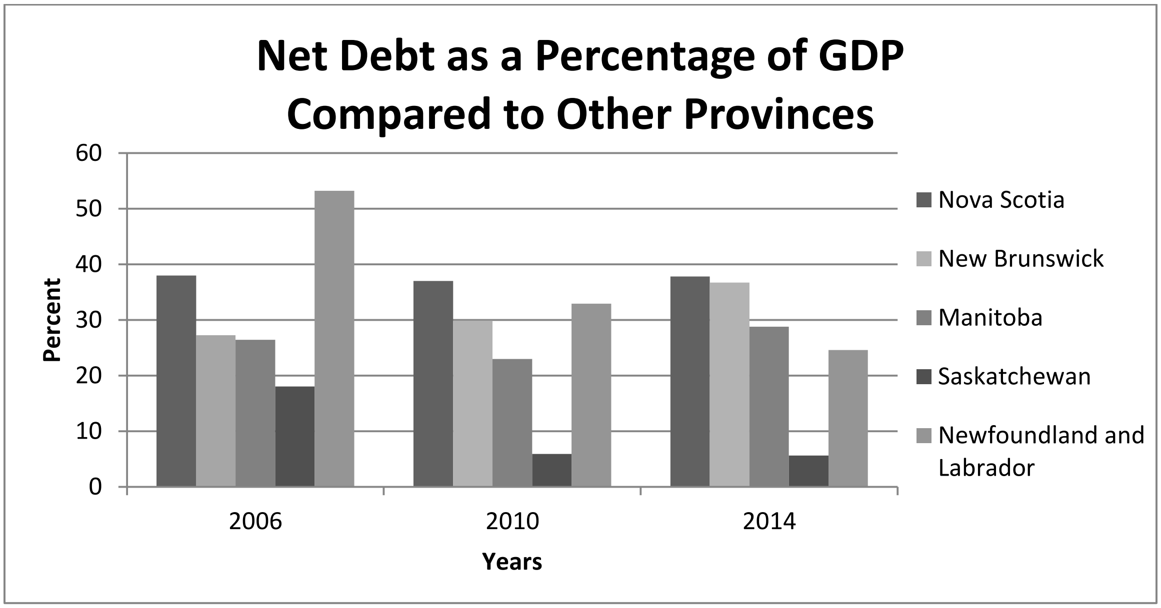
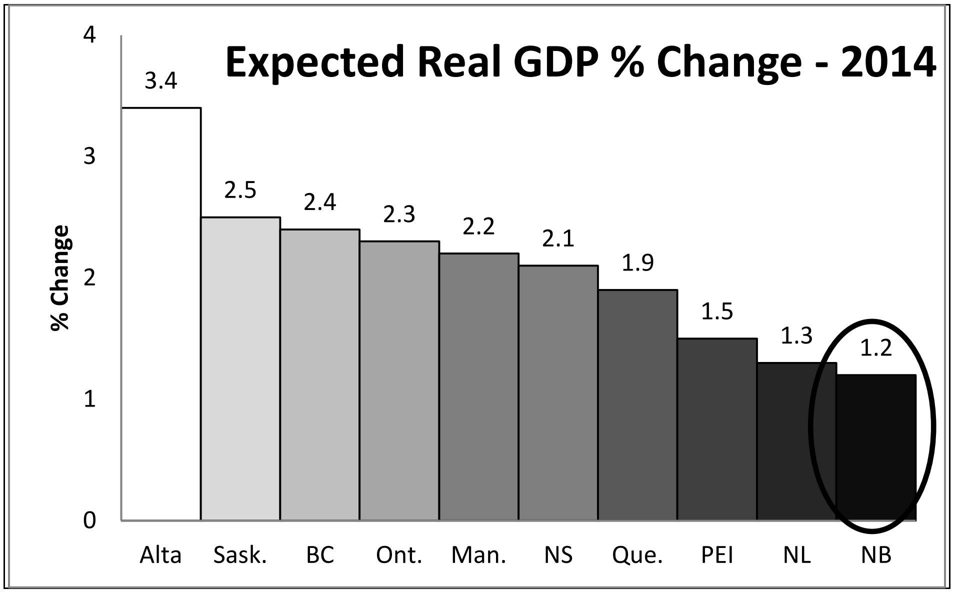


Exhibit 2.15 - Net Debt as a Percentage of GDP Compared to Other Provinces Data

Net Debt as a Percentage of GDP Compared to Other Provinces (percent)				
Province	**2006**	**2010**	**2014**	**% Increase (Decrease) from 2006 to 2014**
Nova Scotia	38.0	37.0	37.8	(0.5%)
New Brunswick	27.3	29.9	36.7	34.4%
Manitoba	26.4	23.0	28.8	9.1%
Saskatchewan	18.0	5.90	5.6	(68.9%)
Newfoundland and Labrador	53.2	32.9	24.6	(53.8%)

2.18 As shown in Exhibits 2.14 and 2.15, New Brunswick had the highest increase of Net Debt as a percentage of GDP from 2006 to 2014, and the second highest Net Debt as a percentage of GDP among comparable provinces for 2014. For the year ended 31 March 2006, New Brunswick's Net Debt as a percentage of GDP was 71.8% of Nova Scotia's; for the year ended 31 March 2014 it was 97.1%.

Exhibit 2.16 - Expected Real GDP % Change - 2014



**Source: 2014-2015 Economic Outlook (Published by Department of Finance, Province of New Brunswick)*

Department of Finance indicates poor economic outlook for New Brunswick

2.19 According to New Brunswick's 2014-2015 Economic Outlook published by the Department of Finance as shown in Exhibit 2.16, New Brunswick is expected to have the lowest real GDP growth of all of the Canadian provinces in 2014. This unfavourable forecast of economic activity is a significant concern given the Province's troubling fiscal challenges.

Net Debt comparison summary

2.20 New Brunswick's Net Debt performance compared to other provinces remains a significant concern. New Brunswick's increase in Net Debt of $4.7 billion from 2006 indicates the need for continued efforts to address the level of Net Debt.

Comments on the Province's Financial Health

2.21 For the past number of years, we included in our annual report a historical trend analysis of the Province's financial condition by looking at measures of sustainability, flexibility and vulnerability.

2.22 Starting in 2009, the Province began reporting some of these measures as part of Volume 1 of Public Accounts (Indicators of Financial Health section). As we commented in previous years, we are pleased to see the Province report this historical information.

2.23 In this section, we report on twelve indicators of financial condition identified by the Public Sector Accounting Board (PSAB) in a Statement of Recommended Practice (SORP). This analysis is intended to give a broader view of the financial health of the Province as the analysis shows trends. The analysis expands on the information reported in the audited consolidated financial statements which only reflect the Province's fiscal status at a point in time.

Assumptions Used

2.24 We have not audited some of the numbers used in our indicator analysis; instead, we are using numbers the Province restated as per Note 18 of the Province's consolidated financial statements. The Province used these restated figures in its Management Discussion and Analysis in Volume 1 of Public Accounts. We have not audited the annualized numbers we obtained from the Province for the years 2005 to 2010. For the 2011- 2014 numbers, we audited the numbers in conjunction with our 2013-2014 audit work.

2.25 In some of the Exhibits that follow, we show five years of comparative figures instead of ten. For these cases, restated numbers for prior years are not available because of changes in accounting policies.

Summary of the Province's Indicators of Financial Condition

2.26 In Exhibit 2.17, we summarize our analysis of the Province's financial indicators. We show the indicators for each element, the purpose of the indicator, the short-term (two year) and long-term (five or ten year) trend, as well as a reference within this chapter of where we discuss the indicator in more detail.

Exhibit 2.17 - Summary of Indicators of Financial Condition

	Indicator	Purpose	Short-term Trend	Term	Long-term Trend[3]	Paragraph
Sustainability	Assets-to-liabilities	Measures extent that government finances its operations by issuing debt	Unfavourable	5 year	Unfavourable	2.30
	Financial asset-to-liabilities	Measures whether future revenues will be needed to pay for past transactions	Unfavourable	5 year	Unfavourable	2.32
	Net Debt-to-total annual revenue	Shows whether more time is needed to pay for past transactions	Unfavourable	10 year	Unfavourable	2.34
	Expense by function-to-total expenses	Shows the trend of government spending over time	Neutral	5 year	Neutral	2.36
	Net Debt-to-GDP	Shows the relationship between Net Debt and the activity in the economy	Unfavourable	10 year	Unfavourable	2.39
	Accumulated deficit–to-GDP	Measures the sum of the current and all prior year operating results relative to the growth in the economy	Unfavourable	5 year	Unfavourable	2.41
	Total expenses-to-GDP	Shows the trend of government spending over time in relation to the growth in the economy	Neutral[1]	10 year	Unfavourable	2.43
Flexibility	Public debt charges-to-revenues	Measures extent that past borrowing decisions limits ability to meet current financial and service commitments	Neutral	10 year	**Favourable**	2.47
	Net book value of capital assets-to-cost of capital assets	Measures the estimated useful lives of tangible capital assets available to provide products /services	Neutral	5 year	Neutral	2.51
	Own-source revenues-to-GDP	Measures extent income is taken out of the economy	Neutral	10 year	Neutral	2.53
Vulnerability	Government transfers-to-total revenues	Measures the dependence on another level of government	**Favourable[2]**	10 year	Mixed	2.60
	Foreign currency debt-to-Net Debt	Measures the government's potential vulnerability to currency fluctuations	**Favourable**	10 year	**Favourable**	2.63

[1] last year was "Favourable"
[2] last year was Unfavourable"
[3] long term trend assessments unchanged in Auditor General Annual Reports 2012-2014

Conclusion

2.27 The long-term and short-term trends continue to show a number of unfavourable financial indicators. The Province's long-term indicators of financial condition have remained unchanged since 2012. The Province's short term indicators of financial condition have seen small changes since the prior year; the short term trend of total expenses-to-GDP has decreased from favourable to neutral, however, we were pleased to see the government transfers-to-total revenues indicator change from unfavourable to favourable in the current year. The majority of unfavourable short term and long term trends are found in the sustainability indicators, however, the favourable trends in the flexibility and vulnerability indicators do indicate improvements.

2.28 We remain concerned about the sustainability indicator trends. The level of Net Debt, now $11.6 billion and the increase of 68.7% since 2006 is undesirable. This pace of Net Debt growth is not sustainable in the long term, and action is required to address this problem. It may eventually impact the Province's ability to meet its existing financial obligations both in respect of its service commitments to the public and financial commitments to creditors, employees and others. We again this year, in addition to addressing the annual deficit, encourage the Province to set and achieve targets for long term net debt control and reduction.

Sustainability Indicators

2.29 Sustainability indicates whether the Province can maintain programs and meet existing creditor requirements without increasing the debt burden on the economy.

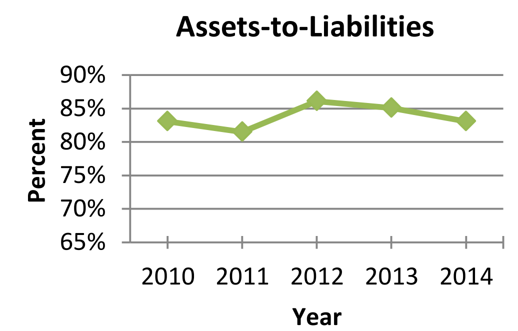
Assets-to-Liabilities

2.30 The sustainability indicator assets-to-liabilities is presented in Exhibit 2.18.

Exhibit 2.18 - Comparison of Assets-to-Liabilities

Comparison of Assets-to-Liabilities

Year ended	**Total assets** ($ millions)	**Total liabilities** ($ millions)	**Total assets/ total liabilities** (percent)
2010	12,045.8	14,485.5	83.2%
2011	13,646.5	16,744.0	81.5%
2012	14,973.9	17,386.9	86.1%
2013	15,933.7	18,738.4	85.0%
2014	16,134.2	19,407.3	83.1%



As restated
** The 2010-2011 amounts are not restated for accounting changes relating to deferred capital contributions and capitalization of computer hardware and software systems.*

2.31 An assets-to-liability indicator below 100% indicates a government has accumulated deficits and has been financing its operations by issuing debt. For the past five years, the Province’s rate was less than 100%. The increase in 2012 compared to previous years relates to an increase in liabilities. The 2010, 2011, 2013 and 2014 trends were unfavourable due to continuous decline. Overall we have assessed the short-term and long-term trend as unfavourable.

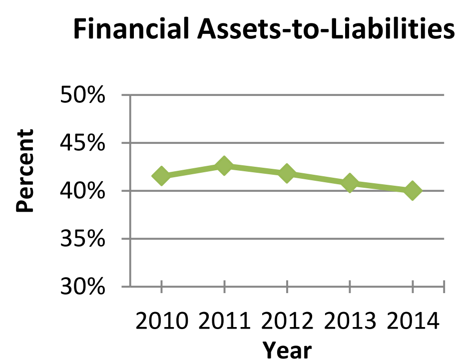
Financial Assets-to-Liabilities

2.32 Another sustainability indicator, financial assets-to-liabilities, is presented in Exhibit 2.19.

Exhibit 2.19 - Comparison of Financial Assets-to-Liabilities

Comparison of Financial Assets-to-Liabilities

Year ended	Total financial assets ($ millions)	Total liabilities ($ millions)	Total financial assets/ total liabilities (percent)
2010	6,014.1	14,485.5	41.5%
2011	7,128.3	16,744.0	42.6%
2012	7,264.7	17,386.9	41.8%
2013	7,653.8	18,738.4	40.8%
2014	7,766.1	19,407.3	40.0%



As restated
** The 2010-2011 amounts are not restated for accounting changes relating to deferred capital contributions and capitalization of computer hardware and software systems.*

2.33 When liabilities exceed financial assets the government is in a Net Debt position, and the implication is that future surpluses will be required to pay for past transactions and events. The Province's percentage has continuously decreased since 2011. We have assessed the short term and long term trend as unfavourable.

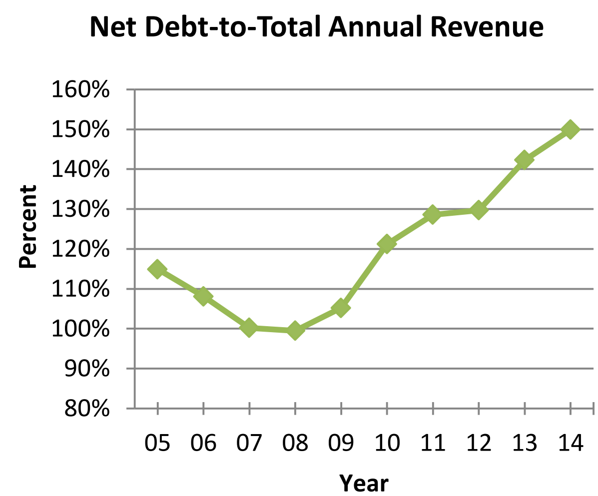
Net Debt-to-Total Annual Revenue

2.34 Net Debt-to-total annual revenue is another indicator of sustainability and is presented in Exhibit 2.20.

Exhibit 2.20 - Comparison of Net Debt-to-Total Annual Revenue

Comparison of Net Debt-to-Total Annual Revenue

Year ended	Net Debt ($ millions)	Total revenue ($ millions)	Net Debt/ total revenue (percent)
2005	6,943.0	6,043.4	114.9%
2006	6,900.6	6,387.1	108.0%
2007	6,761.4	6,756.3	100.1%
2008	7,151.6	7,190.3	99.5%
2009	7,608.0	7,230.9	105.2%
2010	8,628.9	7,120.5	121.2%
2011	9,700.4	7,542.8	128.6%
2012	10,125.8	7,805.9	129.7%
2013	11,084.6	7,787.9	142.3%
2014	11,641.2	7,763.5	149.9%



2.35 Net Debt provides a measure of the future revenue required to pay for past transactions and events. A Net Debt-to-total revenue percentage that is increasing indicates that the Province will need more time to eliminate the Net Debt. The Province's percentage has been increasing over the past six years, most significantly in 2013. The increase in 2013 attributed mainly to the annual deficit and the net capital asset transactions of highways, hospitals, schools and other buildings. Also contributing to the increase was the reduction in income from Government Business Enterprises, reflecting considerably lower net income for New Brunswick Power Corporation, and the reduction in tax revenues related to a weakened economy. The improvements made from 2005-2008 have now been lost. We have assessed this trend as unfavourable.

Expense by Function-to-Total Expenses

2.36 Exhibit 2.21 presents expense by function-to-total expenses.

Exhibit 2.21 - Comparison of Expense by Function-to-Total Expenses

Comparison of Expense by Function-to-Total Expenses										
	2010		2011		2012		2013		2014	
	($ millions)	(%)	($ millions)	(%)	($ millions)	(%)	($ millions)	(%)	($ millions)	(%)
Health	2,595.6	33.2	2,687.0	32.9	2,730.0	33.9	2,786.1	33.6	2,789.9	33.8
Education and Training	1,632.0	20.9	1,723.6	21.1	1,749.3	21.7	1,787.6	21.5	1,821.8	22.0
Social Development	997.2	12.8	1,037.5	12.7	1,029.8	12.8	1,052.8	12.7	1,076.6	13.0
Service of the Public Debt	616.6	7.9	641.4	7.9	661.8	8.2	660.3	8.0	661.9	8.0
Transportation and Infrastructure	381.4	4.9	402.6	4.9	527.6	6.6	547.7	6.6	577.9	7.0
Central Government	682.9	8.7	722.0	8.8	542.2	6.7	636.6	7.7	536.5	6.5
Protection Services	219.7	2.8	260.8	3.2	229.9	2.9	237.3	2.9	235.2	2.8
Economic Development	343.7	4.4	328.4	4.0	257.2	3.2	269.1	3.2	231.4	2.8
Resources	205.8	2.6	215.1	2.6	214.5	2.7	217.4	2.6	212.7	2.6
Labour and Employment	141.5	1.8	141.6	1.7	108.4	1.3	100.5	1.2	118.3	1.4
Total	**7,816.4**	**100.0**	**8,160.0**	**100.0**	**8,050.7**	**100.0**	**8,295.4**	**100.0**	**8,262.2**	**100.0**

2.37 The years ended 31 March 2010 to 31 March 2014 reported deficits. This means that while individual expense trends may have remained steady, this was achieved by incurring a total level of expenses that was in excess of revenue generated in those years. Education and Training and Health's allocation of expenses consume over 55.8% of the total expenses, consistent with prior years.

2.38 The allocation of expenses upon comparing 2014 was relatively stable, however, the impact of New Brunswick's growing Net Debt will need to be closely monitored in the future as the related interest burden on it consumes resources that would otherwise be used to deliver services. We have assessed this indicator as neutral.

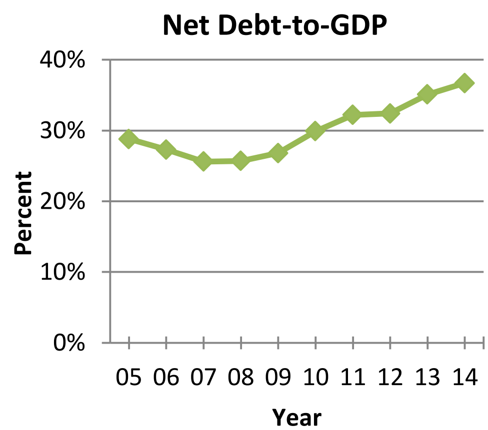
Net Debt-to-GDP

2.39 The sustainability indicator, Net Debt-to-GDP is presented in the Exhibit 2.22.

Exhibit 2.22 - Comparison of Net Debt-to-GDP

Comparison of Net Debt-to-GDP

Year ended	Net Debt ($ millions)	GDP ($ millions)	Net Debt/ GDP (percent)
2005	6,943.0	24,116	28.8%
2006	6,900.6	25,272	27.3%
2007	6,761.4	26,378	25.6%
2008	7,151.6	27,869	25.7%
2009	7,608.0	28,422	26.8%
2010	8,628.9	28,825	29.9%
2011	9,700.4	30,082	32.2%
2012	10,125.8	31,291	32.4%
2013	11,084.6	31,543	35.1%
2014	11,641.2	31,701	36.7%



2.40 This indicator compares the Province's Net Debt, the difference between its liabilities and its financial assets, to its GDP. This ratio declined from 2005 to 2007 indicating that over that time period the level of the Province's debt became less onerous on the economy. The ratio increased from 2008 to 2014 because the rate of growth of Net Debt exceeded the rate of growth in GDP over that time period. In 2014, the ratio reached its highest level since 2005. This means the Net Debt of the Province is increasing faster than the growth in the economy. We have assessed the trend as unfavourable.

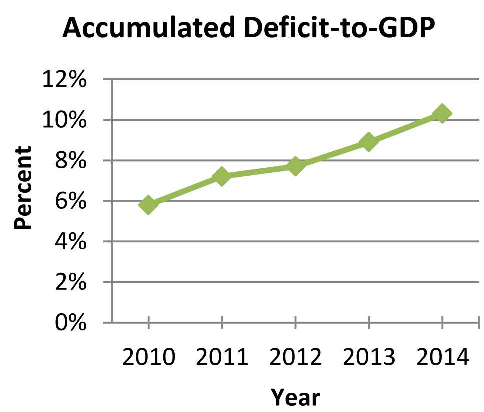
Accumulated Deficit-to-GDP

2.41 In the Exhibit 2.23, we present the sustainability indicator accumulated deficit-to-GDP.

Exhibit 2.23 - Comparison of Accumulated Deficit-to-GDP

Comparison of Accumulated Deficit-to-GDP

Year ended	Accumulated deficit ($ millions)	GDP ($ millions)	Accumulated deficit/GDP (percent)
2010	1,661.3	28,825	5.8%
2011	2,179.2	30,082	7.2%
2012	2,416.5	31,291	7.7%
2013	2,804.7	31,543	8.9%
2014	3,273.1	31,701	10.3%



2.42 The accumulated deficit is the extent to which annual revenues have been insufficient to cover the annual costs of providing services. The information above shows that from 2010 to 2014, the accumulated deficit has increased faster than the growth of the economy. This represents an unfavourable trend.

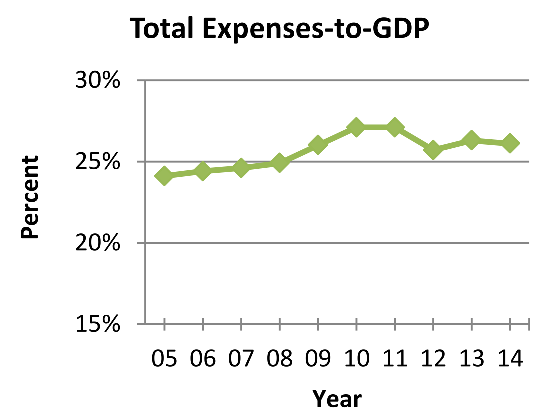
Total Expenses-to-GDP

2.43 Exhibit 2.24 presents the total expenses-to-GDP indicator.

Exhibit 2.24 - Comparison of Total Expenses-to-GDP

Comparison of Total Expenses-to-GDP

Year ended	Total expenses ($ millions)	GDP ($ millions)	Total expenses/GDP (percent)
2005	5,820.2	24,116	24.1%
2006	6,161.8	25,272	24.4%
2007	6,479.0	26,378	24.6%
2008	6,949.2	27,869	24.9%
2009	7,382.9	28,422	26.0%
2010	7,816.4	28,825	27.1%
2011	8,160.0	30,082	27.1%
2012	8,050.7	31,291	25.7%
2013	8,295.4	31,543	26.3%
2014	8,262.2	31,701	26.1%



2.44 Exhibit 2.24 indicates from 2005 to 2008, government expenses were held to about 25% of GDP, however, this percentage has increased and from 2009 to 2014 the percentage averaged 26.4%. This represents an unfavourable long-term trend as expenses are growing faster than the economy is expanding. Although the ratio did decrease in 2012, the following two years show an increase from 2012.We assess the short term trend as neutral and long term trend as unfavourable.

Exhibit 2.25 - Sustainability Indicator Trends

Sustainability Indicator Trends

Sustainability indicator	Short-term trend	Long-term trend
Assets-to-liabilities	Unfavourable	Unfavourable
Financial assets-to-liabilities	Unfavourable	Unfavourable
Net Debt-to-total annual revenue	Unfavourable	Unfavourable
Expense by function-to-total expenses	Neutral	Neutral
Net Debt-to-GDP	Unfavourable	Unfavourable
Accumulated deficit-to-GDP	Unfavourable	Unfavourable
Total expenses-to-GDP	Neutral	Unfavourable

Summary of Sustainability Indicators

2.45 Exhibit 2.25 presents a summary of the Province's sustainability indicators. We note six of seven sustainability indicators are unfavourable in the long term, and five of seven are unfavourable in the short term, and therefore our overall assessment of these trends remains unfavourable. This negative sustainability trend should be of concern to New Brunswickers.

Flexibility Indicators

2.46 Flexibility is the degree to which the government can change its debt or tax burden on the economy to maintain programs and meet existing creditor requirements.

Public Debt Charges-to-Revenues

2.47 One of the most publicized factors which affect the flexibility of governments is the cost of servicing the public debt. This is considered to be an indicator of flexibility, since the Province's first payment commitment is to service its debt, leaving no flexibility in the timing of these payments.

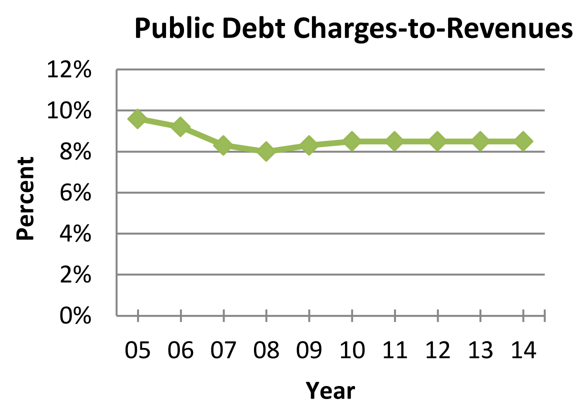
2.48 The cost of servicing the public debt is comprised mainly of interest on the funded debt of the Province. It also includes foreign exchange paid on interest and maturities during the year, the amortization of foreign exchange gains and losses, and the amortization of discounts and premiums which were incurred on the issuance of provincial debt. It does not include principal repayments on the funded debt of the Province.

2.49 In Exhibit 2.26, we present the public debt charges-to-revenues.

Exhibit 2.26 - Comparison of the Public Debt Charges-to-Revenues

Comparison of the Public Debt Charges-to-Revenues

Year ended	Cost of servicing public debt ($ millions)	Revenue ($ millions)	Cost of servicing public debt/ revenue (percent)
2005	579.6	6,043.4	9.6%
2006	590.3	6,387.1	9.2%
2007	558.0	6,756.3	8.3%
2008	575.7	7,190.3	8.0%
2009	601.4	7,230.9	8.3%
2010	607.2	7,120.5	8.5%
2011	641.5	7,542.8	8.5%
2012	661.8	7,805.9	8.5%
2013	660.3	7,787.9	8.5%
2014	661.9	7,763.5	8.5%



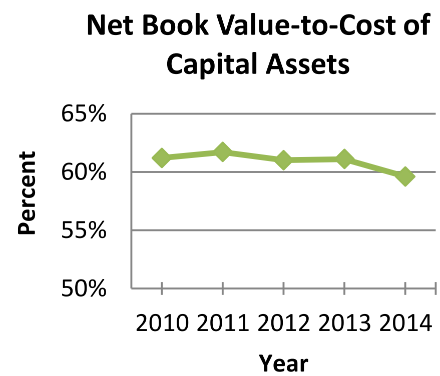
2.50 Exhibit 2.26 shows that the cost of servicing the public debt as a percentage of the Province's total revenues is significantly lower in the year ended 31 March 2014 than it was in the year ended 31 March 2005. This means that the Province is spending proportionately less of its current year revenue to cover debt charges resulting in more current year revenue available to cover services to the public. For the past five years, the ratio has remained the same and we are assessing the short-term trend as neutral. We are assessing the long-term trend as favourable as the current year's ratio is less than the ratio in 2005. Although we are assessing this indicator as favourable, caution is needed when looking at this indicator. The cost of servicing the Province's debt is increasing in a time when interest rates have declined and the Province's debt is increasing significantly.

Net Book Value of Capital Assets-to-Cost of Capital Assets

2.51 We present the net book value of capital assets-to-cost of capital assets in the Exhibit 2.27.

Exhibit 2.27 - Comparison of Net Book Value of Capital Assets-to-Cost of Capital Assets

Comparison of Net Book Value of Capital Assets-to-Cost of Capital Assets			
Year ended	**Net book value** ($ millions)	**Capital cost** ($ millions)	**Net book value/ capital cost** (percent)
2010	6,706.0	10,959.3	61.2%
2011	7,241.7	11,733.2	61.7%
2012	7,452.5	12,221.3	61.0%
2013	7,977.6	13,065.3	61.1%
2014	8,018.5	13,451.2	59.6%



2.52 This data indicates that the Province's inventory of capital assets as at 31 March 2014 has 59.6% of its average useful life remaining. This roughly means that on average any Provincial assets that were originally expected to be useable for ten years still had just under six years of remaining useful life at 31 March 2014, and assets with original useful lives of twenty years were still considered useable for just under twelve years on average. As the ratios have remained relatively the same over the past five years, we are assessing the short-term and long-term trends as neutral.

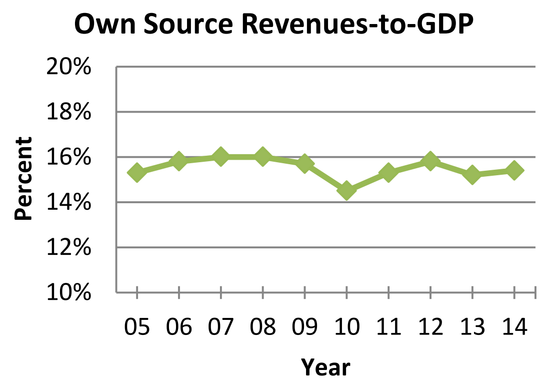
Own Source Revenues-to-GDP

2.53 We present own source revenues-to-GDP in Exhibit 2.28.

Exhibit 2.28 - Comparison of Own Source Revenues-to-GDP

Comparison of Own Source Revenues-to-GDP

Year ended	Own source revenues ($ millions)	GDP ($ millions)	Own source revenues/ GDP (percent)
2005	3,688.6	24,116	15.3%
2006	3,994.2	25,272	15.8%
2007	4,225.4	26,378	16.0%
2008	4,469.7	27,869	16.0%
2009	4,467.3	28,422	15.7%
2010	4,179.7	28,825	14.5%
2011	4,612.5	30,082	15.3%
2012	4,931.7	31,291	15.8%
2013	4,787.4	31,543	15.2%
2014	4,888.8	31,701	15.4%



2.54 The own source revenues-to-GDP indicator measures the extent to which the Province is raising its revenue through extracting it from the provincial economy. If the ratio increases, more of the Province's revenue is generated from the provincial economy. For example, an increase in this ratio could result if the Province increased taxes. If the ratio decreases, less of the Province's revenue is generated from the provincial economy. A decreasing ratio increases the Province's ability to raise taxes, thus, making the Province more flexible in how it can generate revenue. Generally, this ratio has stayed the same over the long-term and we have assessed this indicator as neutral.

2.55 There was a decrease in the year 2010 mostly as a result of a large loss by the then New Brunswick Electric Finance Corporation (EFC) (now amalgamated with New Brunswick Power Corporation). In that year, the reduction in own source revenue was not as a result of lower fees or taxes.

2.56 In 2014, own source revenue increased by $101.4 million. The most significant source of this increase was an increase of taxes of $53.2 million relating to personal and corporate income tax increases. The next significant source of this increase relates to a $42.9 million increase in investment income from New Brunswick Power Corporation.

2.57 A note of caution should be taken when looking at this indicator for the last five years. The Province incurred deficits which means expenses were higher than the revenue generated.

Exhibit 2.29 - Flexibility Indicator Trends

Flexibility Indicator Trends		
Flexibility indicator	**Short-term trend**	**Long-term trend**
Public debt charges-to-revenues	Neutral	Favourable
Net book value of capital assets-to-cost of capital assets	Neutral	Neutral
Own source revenues-to-GDP	Neutral	Neutral

Summary of Flexibility Indicators

2.58 As summarized in Exhibit 2.29, our overall assessment on flexibility in the short term and long term is largely neutral. However, caution should be used in interpreting these results. This result was achieved in a period where the Province incurred its sixth consecutive deficit and the cost of servicing the Province's debt was increasing (i.e. in a period when interest rates are generally decreasing and the Province's debt load is increasing).

Vulnerability Indicators

2.59 Vulnerability is the degree to which a government is dependent on sources of funding outside its control or influence.

Government Transfers-to-Total Revenues

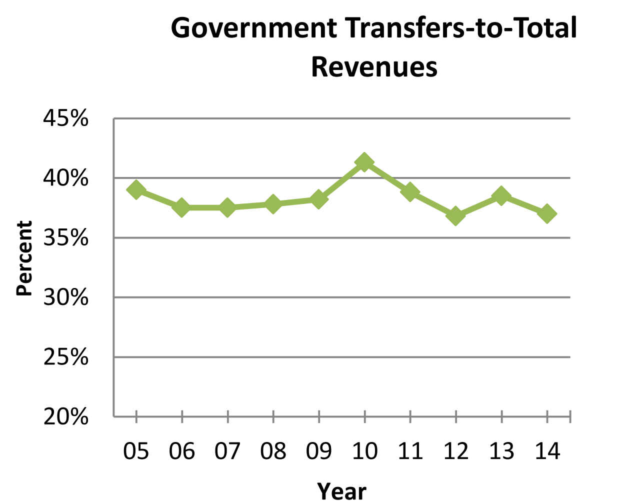
2.60 By comparing the proportion of total revenue that comes from the federal government to the total revenue of the Province, we get a measure of the degree to which the Province is dependent on the federal government. If that dependence increases, the Province is more vulnerable to funding decisions made by the federal government.

2.61 Exhibit 2.30 presents the comparison of government transfers-to-total revenues.

Exhibit 2.30 - Comparison of Government Transfers-to-Total Revenues

Comparison of Government Transfers-to-Total Revenues

Year ended	Federal government transfer revenue ($ millions)	Total revenue ($ millions)	Federal government transfer revenue/ total revenue (percent)
2005	2,354.8	6,043.4	39.0%
2006	2,392.9	6,387.1	37.5%
2007	2,530.9	6,756.3	37.5%
2008	2,720.6	7,190.3	37.8%
2009	2,763.6	7,230.9	38.2%
2010	2,940.8	7,120.5	41.3%
2011	2,930.3	7,542.8	38.8%
2012	2,874.2	7,805.9	36.8%
2013	3,000.5	7,787.9	38.5%
2014	2,874.7	7,763.5	37.0%



2.62 Exhibit 2.30 shows the Province's reliance on federal government transfers decreased from 2010 to 2012, and increased after 2012. However, revenues decreased in part in 2014 due to a one-time capital revenue received in 2013 related to the Route One Gateway Project. The reliance on federal transfers decreased in 2014 and has remained relatively consistent with prior years. Thus we are assessing the short-term trend as favourable and the long-term trend as mixed.

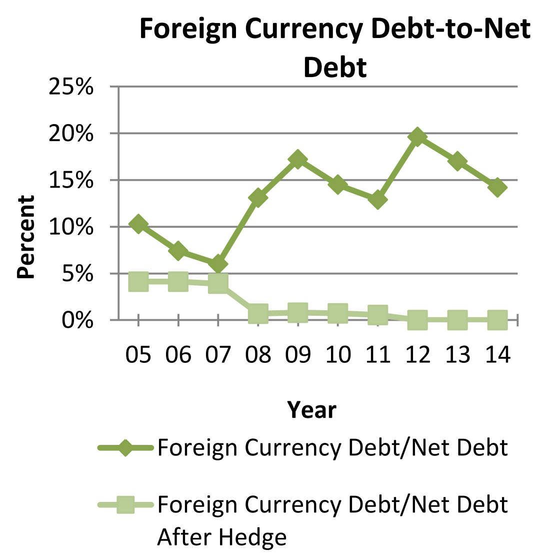
Foreign Currency Debt-to-Net Debt

2.63 The foreign currency debt-to-net debt indicator measures the Province's potential vulnerability to currency fluctuations and is presented in Exhibit 2.31.

Exhibit 2.31 - Comparison of Foreign Currency Debt-to-Net Debt

Comparison of Foreign Currency Debt-to-Net Debt

Year ended	Foreign currency debt ($ millions)	Net Debt ($ millions)	Foreign currency debt/ Net Debt(per cent)	Foreign currency debt/ Net Debt after hedge (percent)
2005	717.5	6,943.0	10.3%	4.1%
2006	512.9	6,900.6	7.4%	4.2%
2007	403.5	6,761.4	6.0%	3.9%
2008	937.0	7,151.6	13.1%	0.7%
2009	1,304.8	7,608.0	17.2%	0.8%
2010	1,255.8	8,628.9	14.2%	0.7%
2011	1,247.3	9,700.4	12.9%	0.6%
2012	1,986.8	10,125.8	19.6%	0.0%
2013	1,888.5	11,084.6	17.0%	0.0%
2014	1,656.9	11,641.2	14.2%	0.0%



2.64 The above information shows that the Province's foreign currency debt has increased from 2007 to 2012; however foreign currency debt decreased in 2013 and 2014. The risk of exposure to foreign currency fluctuations is offset by the Province's hedging strategy. The Province uses several alternatives to reduce (hedge) risk associated with debt repayable in foreign currencies:

- purchasing assets denominated in foreign currencies for the Province's sinking fund;
- entering into swap agreements which allows repayment of the debt and interest payments in Canadian dollars; and
- entering into forward contracts (which allow the Province to purchase foreign currency at a stipulated price on a specified future date).

2.65 From Exhibit 2.31, we see the risk of exposure to foreign currency fluctuations has decreased significantly over time. Because of the effectiveness of the Province's hedging strategy, we assess this indicator as favourable.

Exhibit 2.32 - Vulnerability Indicator Trends

Vulnerability Indicator Trends		
Vulnerability indicator	**Short-term trend**	**Long-term trend**
Government transfers-to-total revenues	Favourable	Mixed
Foreign currency debt-to-net debt	Favourable	Favourable

Summary of Vulnerability Indicators

2.66 As summarized in Exhibit 2.32, the Province's vulnerability exposure is mixed. In years when EFC (now amalgamated with NB Power) generated income through its investment in NB Power, the Province's reliance on federal revenue lessened and this indicator improves. As well, there is reliance on the federal government in certain years to assist in funding major infrastructure projects. Also of note is that the Province is effectively managing and controlling its exposure to fluctuations in foreign currency.

Comments on Significant Trends Observed in the Province's Consolidated Financial Statements

2.67 In this section, we discuss significant trends we have observed in the Province's consolidated financial statements. We have highlighted these trends to raise public awareness and to provide legislators with an independent assessment of the areas we believe should be a focus for the government.

Deficit

2.68 For the year ended 31 March 2014, the Province reported a deficit of $498.7 million. This is a decrease of $8.8 million from the $507.5 million deficit reported for the year ended 31 March 2013.

2.69 Exhibit 2.33 shows, at a high level, the reasons for the change in the deficit from 31 March 2013 to 31 March 2014.

Exhibit 2.33 - Analysis of Deficit Increase

Analysis of Deficit Increase	
	(millions)
2013 Deficit	$(507.5)
Increase in provincial source revenue	101.4
Decrease in federal source revenue	(125.8)
Decrease in expense	33.2
2014 Deficit	**$(498.7)**

2.70 Increases in provincial source revenue are mainly attributable to an increase of $146.5 million of personal income tax and an increase of $32.2 million of income from Government Business Enterprises (primarily due to New Brunswick Power Corporation), offset by a decrease in Harmonized Sales Tax revenue of $107.8 million, as reported in the Province's 2014 audited consolidated financial statements.

2.71 Changes in federal source revenue are explained by the following:

- a decrease of $35.7 million in fiscal equalization payments, due to a narrowing of fiscal disparities between New Brunswick and the national average;
- a decrease of $144.8 million in conditional grants due to a one-time capital funding received in 2013 related to the Route One Gateway Projects and finally;
- an offset, however, is represented by an increase of $54.7 million in unconditional grant revenue primarily due to the legislated growth in the federal cash funding for the Canada Health Transfer and the Canada Social Transfer, as well as positive adjustments related to population data.

2.72 Total expenses have decreased by $33.2 million. The most significant decrease in expenses is $100.1 million in Central Government. This decrease is in part due to a decrease in expense of $56.4 million for the early retirement benefit plan upon comparison with the prior year, as the prior year figures contained a higher expense to account for mortality and discount rate changes. This is offset by an adjustment of $21.9 million in the current year for a one-time expense reduction to recognize the net pension asset of the New Brunswick Power Corporation at conversion to the Public Service Shared Risk Plan. Significant increases were noted in Education and Training ($34.2 million) and Transportation and Infrastructure ($30.2 million) during the year. The increase in Education and Training was mainly due to additional investments and salaries in K-12 education, where the increase in Transportation and Infrastructure was attributed to increased amortization and expenses in a number of the department's programs.

Expenses

2.73 Exhibit 2.34 shows the one year growth rate and the average growth rate for the past three years.

Exhibit 2.34 - Expense Trends by Function (percentage)

Expense Trends by Function				
Function	**2012 Growth Rate (%)**	**2013 Growth Rate (%)**	**2014 Growth Rate (%)**	**Three year average growth rate (%)**
Education and Training	1.5	2.2	**1.9**	1.9
Health	1.6	2.0	**0.1**	1.2
Service of the Public Debt	3.2	(0.2)	0.2	1.1
Social Development	(0.7)	2.5	2.3	1.4
Transportation and Infrastructure	31.0	3.8	5.5	**13.4**
Protection Services	(11.9)	3.2	(0.9)	(3.2)
Resources	(0.2)	(2.1)	(2.2)	(1.5)
Central Government	(24.9)	16.9	**(15.7)**	(7.9)
Labour and Employment	(23.5)	(7.3)	**17.7**	(4.4)
Economic Development	(21.7)	5.2	**(14.0)**	(10.2)
Total	**(4.6)**	**2.6**	**(0.5)**	**(0.8)**

2.74 Exhibit 2.34 shows the Province's one year expense growth rate has decreased compared to 2013 by 0.5%. In fiscal 2014, six out of ten functions showed an increase in the one year growth rate. Four of ten function areas show a negative growth which implies cost reductions were realized. The average three year expense growth rate for 2014 was (0.8%). This is an improved result over the prior year average three year expense growth rate of 0.9%.

2.75 We noted the 2014 expense growth rate has slowed in the Health and Education and Training departments, the largest expense function areas, compared to the 2013 growth rate.

2.76 However, Exhibit 2.34 shows Labour and Employment experiencing the largest one year growth rate in 2014 of 17.7%, primarily due to increased uptake in the Workforce Expansion and Training Skills Development programs. However, the two significant negative one year growth rates (expense reductions) were in Central Government (15.7%) and Economic Development. (14.0%)

2.77 In comparing the three year average growth rate, Transportation and Infrastructure experienced the largest three year average growth rate of 13.4%. However, a positive trend exists where five departments show the three year average growth rate decreasing. These decreasing growth rates illustrate progress to reduce or restrain spending in expense functions. It should be noted that regardless of the current restraint efforts of government, as illustrated in Exhibit 2.34, the Province has experienced deficits and continued Net Debt growth.

Revenue

2.78 Exhibit 2.35 shows the one year growth rate and the average growth rate of revenue for the past three years.

2.79 Total revenues have decreased by $24.4 million. This is attributable to decreased revenue from federal sources of $125.8 million and an offsetting increase in revenue from provincial sources of $101.4 million.

Exhibit 2.35 - Revenue Trends by Source

Revenue Trends by Source							
	($ millions)			(% percentages)			
Source	**2012 Revenue Amount**	**2013 Revenue Amount**	**2014 Revenue Amount**	**2012 Growth Rate**	**2013 Growth Rate**	**2014 Growth Rate**	**Three year average growth rate**
Provincial Sources							
Taxes	3,574.0	3,542.1	3,595.3	4.2	(0.9)	1.5	1.6
Licenses and Permits	138.8	144.6	148.7	3.3	4.2	2.8	3.4
Royalties	89.3	86.1	90.9	2.1	(3.6)	5.6	1.4
Other Provincial Revenue	903.6	793.9	849.4	24.3	(12.1)	7.0	**6.4**
Sinking Fund Earnings	225.6	220.7	204.5	0.9	(2.2)	(7.3)	(2.9)
Federal Sources							
Fiscal Equalization Payments	1,632.6	1,597.7	1,562.0	(1.8)	(2.1)	(2.2)	(2.0)
Unconditional Grants	865.7	894.2	948.9	3.9	3.3	6.1	4.4
Conditional Grants	375.9	508.6	363.8	(11.3)	35.3	**(28.5)**	(1.5)
Total	**7,805.90**	**7,787.9**	**7,763.5**	**25.60**	**21.90**	**(15.0)**	**10.8**
Average Growth Rate	**-**	**-**	**-**	**3.2**	**2.7**	**(1.9)**	**1.4**

2.80 Exhibit 2.35 shows the Province's 2014 revenue growth rate was negative 1.9% with a three year average growth rate of 1.4%. The 2014 growth rate shows a notable decrease in conditional grants revenue relating to one-time funding in 2013 for Route One Gateway Project of $117 million.

2.81 We noted the 2014 negative growth in revenue is concerning especially given the 2014 expected unfavorable GDP growth in New Brunswick as forecasted by the Department of Finance. We also note the largest three year average growth percent of 6.4% (other provincial revenue) had only a modest impact on the Province's fiscal results due to the relatively small dollar value ($849.4 million) in this revenue category.

Other Provinces – Revenue and Expense Comparison

2.82 Exhibit 2.36 shows the trend of gross revenues and gross expenses when compared to other provinces. Data from other provinces is taken from the audited summary financial statements of the individual provinces.

Exhibit 2.36 - Revenue and Expense (Comparison to other provinces)

Revenue and Expense (Comparison to other provinces) ($ millions)								
	Gross Revenues				Gross Expenses			
	2012	2013	2014	% Increase from 2012 to 2014	2012	2013	2014	% Increase from 2012 to 2014
New Brunswick	7,805.9	7,787.9	7,763.5	(0.5%)	8,050.7	8,295.2	8,262.4	2.6%
Nova Scotia	9,760.3	10,104.1	10,035.1	2.8%	10,019.3	10,407.7	10,714.0	6.9%
Saskatchewan	12,817.0	14,323.0	14,418.0	12.5%	13,711.0	14,285.0	13,829.0	0.9%
Manitoba	13,688.0	13,614.0	14,214.0	3.8%	14,689.0	14,174.0	14,736.0	0.3%
Newfoundland and Labrador	8,812.0	7,505.5	7,487.5	(15.0%)	7,838.0	7,700.5	7,786.0	(0.5%)

2.83 We note that over the last three years within this group, New Brunswick has had a slight decrease in revenue of 0.5%. Three of four other provinces have experienced revenue increases. We also note over the last three years New Brunswick's expenses have increased only 2.6 %, however in the group reviewed this appears high (one province reduced expenses and two provinces growth rates were lower). Over the last three years we also note New Brunswick shows the second highest increase in gross expenses.

2.84 While much has been done to address government expense growth, action is needed still to address New Brunswick's structural deficit and continued net debt growth. We look forward to seeing the new Net Debt reduction targets achieved or exceeded as work continues to address New Brunswick's fiscal challenges.

Chapter 3
Province of New Brunswick Audit: Observations on Pension Plans

Contents

Province of New Brunswick Audit: Observations on Pension Plans

Introduction

3.1 As the accounting for pensions is material to the Province's consolidated financial statements and involves complex accounting issues, we have presented our observations on these topics in a separate chapter of our Report.

Pension Plans - Impacts on the Province

3.2 In prior years market fluctuations and other pension related issues have exposed the Province to volatility in its financial results in the Province's financial statements. For the year ended 31 March 2014 pension expense of $365.4 million was recorded. In addition, complex accounting issues for Shared Risk Pension Plans have been encountered in the past two years. The following paragraphs illustrate these trends, as well as discuss other impacts on the Province associated with the plans.

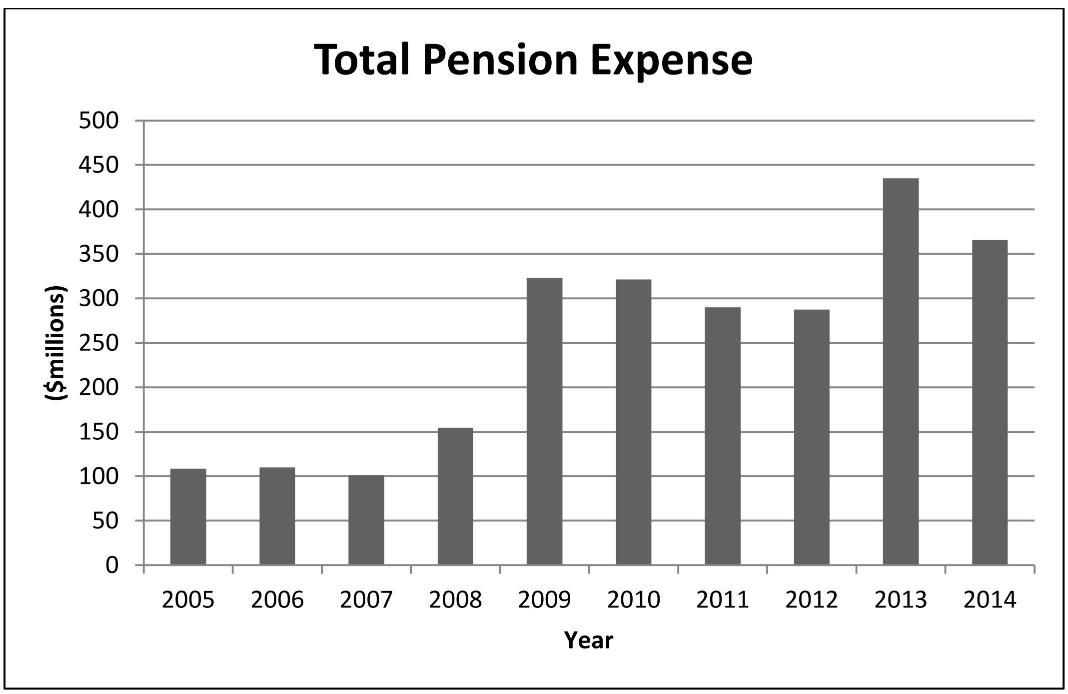
Pension expense growth and volatility

3.3 Exhibit 3.1 provides details of the Province's total pension expense for the past ten years. For purposes of illustrating the potential volatility of this figure, a longer term approach of ten years has been provided.

Exhibit 3.1 - Components of Pension Expense

Components of Pension Expense ($ millions)										
	2005	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**
Employer's share of pension benefits earned	124.1	117.0	126.1	133.8	146.1	131.6	137.4	148.9	177.4	196.0
Net interest expense (revenue)	17.6	30.9	0.4	(9.1)	20.6	118.2	52.9	32.0	62.7	70.4
Plan amendments	-	-	5.9	-	-	-	-	-	-	(11.2)
Amortization of adjustments	(31.8)	(40.3)	(31.2)	30.3	159.7	87.1	99.7	106.5	194.9	132.1
Change in valuation adjustment	(1.5)	2.3	(0.1)	(0.5)	(3.3)	(15.5)	-	-	-	-
NB Power adjustment on shared risk plan conversion	-	-	-	-	-	-	-	-	-	(21.9)
Total pension expense	**108.4**	**109.9**	**101.1**	**154.5**	**323.1**	**321.4**	**290.0**	**287.4**	**435.0**	**365.4**

Exhibit 3.2 - Total Pension Expense



3.4 Exhibits 3.1 and 3.2 highlight the significant increase in the annual pension expense over the ten year period as well as the volatility of the expense. In the year ended 31 March 2005, the pension expense was $108.4 million. By way of contrast, in the year ended 31 March 2014, the pension expense was $365.4 million, an increase of $257.0 million when compared to 2005. The pension expense decreased in 2014 compared to 2013 in part due to a decrease in expense of $56.4 million for the early retirement benefit plan upon comparison with the prior year, as the prior year figures contained a higher expense to account for mortality and discount rate changes. This is offset by a one-time adjustment of $21.9 million to recognize the net pension asset of the New Brunswick Power Corporation at conversion to the Public Service Shared Risk Plan.

3.5 Exhibit 3.3 compares the annual pension expense to the amount of contributions made by the Province to the various pension plans.

Exhibit 3.3 - Pension Expense and Contributions

Pension Expense and Contributions ($ millions)										
	2005	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**
Pension expense	108.4	109.9	101.1	154.5	323.1	321.4	290.0	287.4	435.0	365.4
Employer contributions	223.2	236.4	257.7	272.8	288.6	307.8	313.3	327.0	350.8	216.5
Excess (deficiency) of employer contributions over pension expense	114.8	126.5	156.6	118.3	(34.5)	(13.6)	23.3	39.6	(84.2)	(148.9)

3.6 Exhibit 3.3 shows that for four of the past ten years, the Province's contributions to its various pension plans have been less than the annual pension expense, whereas for six of the past ten years the amount of employer contributions exceeded the amount of the pension expense. Over the past ten years, the province has contributed $297.9 million more than the pension expense.

3.7 The year to year differences are largely due to the legislated and actuarial funding requirements of the plans being different than the measurement of pension expense as required by Public Sector Accounting Standards. Funding requirements are intended to ensure there will be sufficient funds in the plans to pay pension benefits while the pension expense is intended to measure the net cost of pension benefits earned by employees during the year.

Pension contributions for the Province's largest plans

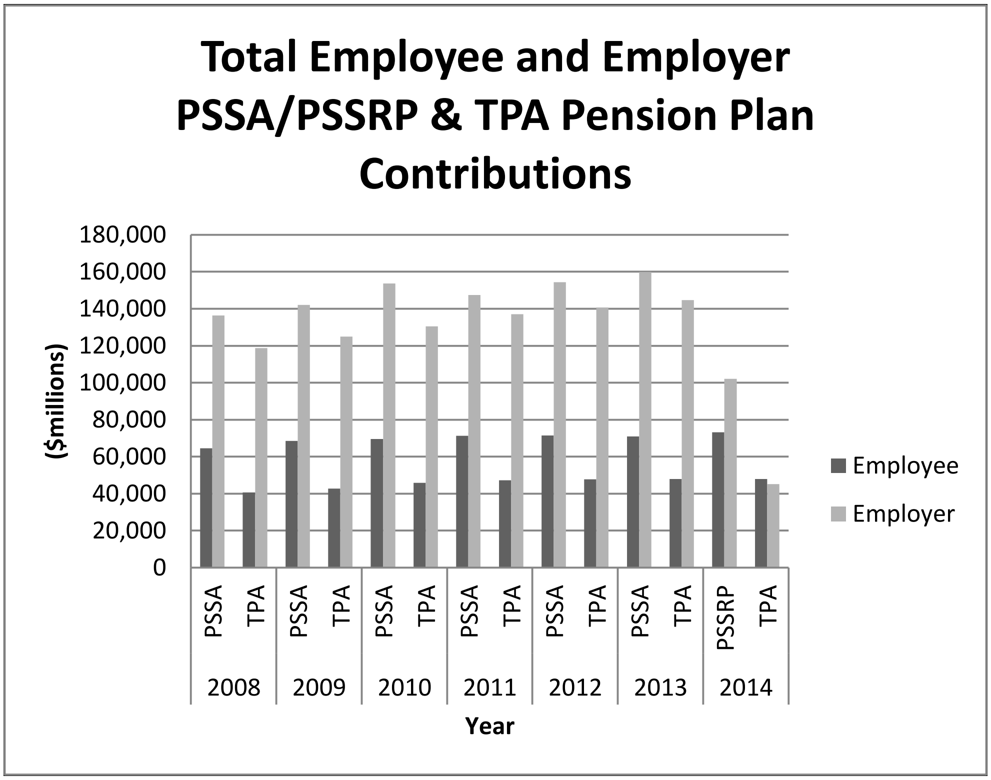
3.8 Further details on pension contributions from 2008 to 2014 for the Province's two largest plans, the Public Service Superannuation Plan (PSSA), now the Public Service Shared Risk Plan (PSSRP) and the Teachers' Pension Plan (TPA) are found in Exhibits 3.4 and 3.5.

Exhibit 3.4 - Pension Contributions for PSSRP/PSSA and TPA Plans

Pension Contributions for PSSRP/PSSA and TPA Plans ($ millions)							
		Employee Contributions	Employer Contributions[1]			Total Employee and Employer Contributions	Ratio of Employer to Employee Contributions
			Normal	Special Payments	Total Employer Contributions		
2014	**PSSRP**	73.1	102.1	-	102.1	175.3	1.40
	TPA	47.7	46.5	-	46.5	94.2	0.97
2013	**PSSA**	70.9	92.1	67.9	160.0	230.9	2.26
	TPA	47.9	46.1	98.6	144.8	192.6	3.02
2012	**PSSA**	71.5	89.4	64.9	154.3	225.8	2.16
	TPA	47.8	46.4	94.4	140.7	188.6	2.94
2011	**PSSA**	71.2	84.3	63.2	147.5	218.7	2.07
	TPA	47.3	45.1	91.9	137.0	184.3	2.90
2010	**PSSA**	69.6	92.8	61.0	153.7	223.3	2.21
	TPA	45.9	41.9	88.6	130.5	176.4	2.84
2009	**PSSA**	68.6	83.6	58.5	142.1	210.7	2.07
	TPA	42.7	39.9	85.0	124.9	167.6	2.93
2008	**PSSA**	64.6	80.0	56.4	136.4	201.0	2.11
	TPA	40.6	36.7	81.9	118.6	159.2	2.92
Total 2008-2014	**PSSA**	**489.5**	**624.3**	**371.9**	**996.1**	**1,485.7**	**2.03**
	TPA	**319.9**	**302.6**	**540.4**	**843.0**	**1,162.9**	**2.64**

[1] *PSSA Employer contributions include contributions from the Province, Crown Corporations and other participants.*

Exhibit 3.5 - Total Employee and Employer (PSSA/PSSRP & TPA) Pension Plan Contributions



The 2014 elimination of special payments to pension plans resulted in an estimated annual cash flow savings of over $150.0 million

3.9 We note that total employer contributions decreased significantly for both the PSSA/PSSRP and TPA plans in fiscal 2014. Employer's contributions for the TPA plan decreased $98.3 million (68% decrease) and employer contributions to the PSSA/PSSRP decreased by $57.9 million (36% decrease). This is a significant change and noteworthy since, in the PSSA/PSSRP's case, this was due to the adoption of a shared risk pension structure while in the case of the TPA plan, no agreement on shared risk had been reached at the time however the Province decided to cease making special payments to the plan. It was determined by the Department of Finance there was no legal requirement to continue these special payments. In both cases, the decision by the Province to stop making special payments to these pension plans was significant. The total cash flow savings to the Province of eliminating special payments to pension plans in fiscal 2014 using an average of the prior six years as a comparison basis was $152.1 million. These savings will compound over time (estimated as billions of dollars of cash flow savings).

3.10 As shown in Exhibit 3.4, TPA employee contributions remained relatively unchanged since last year decreasing less than 1%. PSSRP employee contributions increased by 3% year over year mostly due to an increase in purchase of service contributions of $2.8 million. This resulted in the ratio of employer to employee contributions falling significantly from 3.02 in 2013 to 0.97 in 2014 for the TPA plan and the PSSRP plan ratio falling from 2.26 to 1.40.

Funding status of the TPA plan

3.11 The most recent (April 1, 2012) TPA plan actuarial valuation for funding purposes showed an unfunded liability of approximately $595 million or 87.5% funded (2011 = $458 million or 89.8% funded).

At April 1, 2012 the PSSA plan showed an unfunded liability of $1.022 billion or 83.6%

3.12 Specific to the PSSA plan, the April 1, 2012 actuarial valuation for funding purposes showed an unfunded liability of approximately $1.022 billion or 83.6% funded (2011 = $507 million or 90.9% funded).

At January 1, 2014 upon conversion to PSSRP the plan was fully funded at 100.3%

3.13 Upon conversion to the PSSRP plan structure on January 1, 2014 the unfunded liability (for purposes of calculating the funding policy valuation funded status) decreased from the April 1, 2012 value by $1.041 billion as a result of the conversion to the PSSRP structure. The new funding policy valuation as at January, 1, 2014 showed a valuation excess (surplus) of $18.9 million. The funding policy valuation as of January 1, 2014 showed the plan was 100.3% funded.

3.14 This change in funded status compared to April 1, 2012 figures was achieved through significant plan assumption changes for purposes of the funding policy valuation such as:

- removal of automatic indexing and no anticipation of salary increases for purposes of the PSSRP funding policy valuation;
- change in the retirement age assumption due to a change in the retirement age reduction factor. This results in more years with employees working and contributing to the plan and less years receiving pension benefits. Under PSSA plan structure there was no reduction factor to retire upon or after age 60 and if employees

retire earlier than age 60 a 3% reduction factor per year applied. Under the new PSSRP plan structure there is no reduction factor for employees to retire upon or after age 65 and if employees retire earlier than age 65, a 5% reduction factor per year will be applied (for post January 1, 2014 service);

- discount rate change from 6.6% as of April 1, 2012 to 4.75% January 1, 2014 to reflect expected changes in the pension asset mix in order to reduce possible risk exposure and volatility on asset values. As a result, pension asset investment returns are expected to be more stable/lower and derive from a more conservative asset portfolio.

3.15 It should be noted that the funding policy valuation under the PSSRP considers a "termination" value approach. The termination value calculates the amount a member is entitled to if they leave the plan prior to retirement. This obligation is measured based on services accrued at the valuation date and accordingly future salary increases and future indexing of benefits are excluded from this calculation. It is important to note the measurement process differs due to the nature of the valuation. Therefore the PSSRP funding policy valuation cannot be directly compared with the PSSA valuation techniques used in past, but it serves as a reference point to understand the financial impacts of the new PSSRP structure.

At January 1, 2014 the PSSRP 15 year open group funded ratio was 121.5%

3.16 It is also of note that in the PSSRP plan environment there is an important new measurement of the plan's financial performance. The 15 year open group funded ratio is used extensively in the PSSRP funding policy to determine the actions to be taken by the Trustees for future indexing decisions and future changes to contributions or benefits. It is calculated using an asset value that includes the present value of the next 15 years of any excess contributions above the normal cost of the base benefit. As at January 1, 2014 the PSSRP's 15 year open group funded ratio was 121.5%.

3.17 Other shared risk plans' open group funded ratios we found publicly available were the City of Saint John at 114.3% as of January 1, 2014 and the CUPE Employees of N.B. Hospitals, Local 1252 at 114.0% as of July 1, 2012. As the open group funded ratio is part of the required reporting to plan members in a shared risk environment in New Brunswick, we were surprised to note during our audit of the Province that the conversion plan and initial actuarial valuation report (which initially reports the open group funded ratio) was not yet available for the Shared Risk Plan for Certain Bargaining Employees of New Brunswick Hospitals. These documents were later filed with the Superintendent of Pensions on December 31, 2014.

Impact on the Province's employees of recent PSSA plan changes

3.18 As per the Province’s March 31, 2014 consolidated financial statements there are 19,419 active contributors and 14,672 pensioners of the PSSRP/PSSA plan. Details of how PSSA plan changes impact the Province's employees are illustrated in Exhibits 3.6 and 3.7.

3.19 We considered three particular employee scenarios for employees at the beginning of their career, middle of their career and near retirement to illustrate the impacts of the pension plan changes. Exhibit 3.6 shows the results of our analysis. Exhibit 3.7 graphs the information for one of the scenarios in Exhibit 3.6.

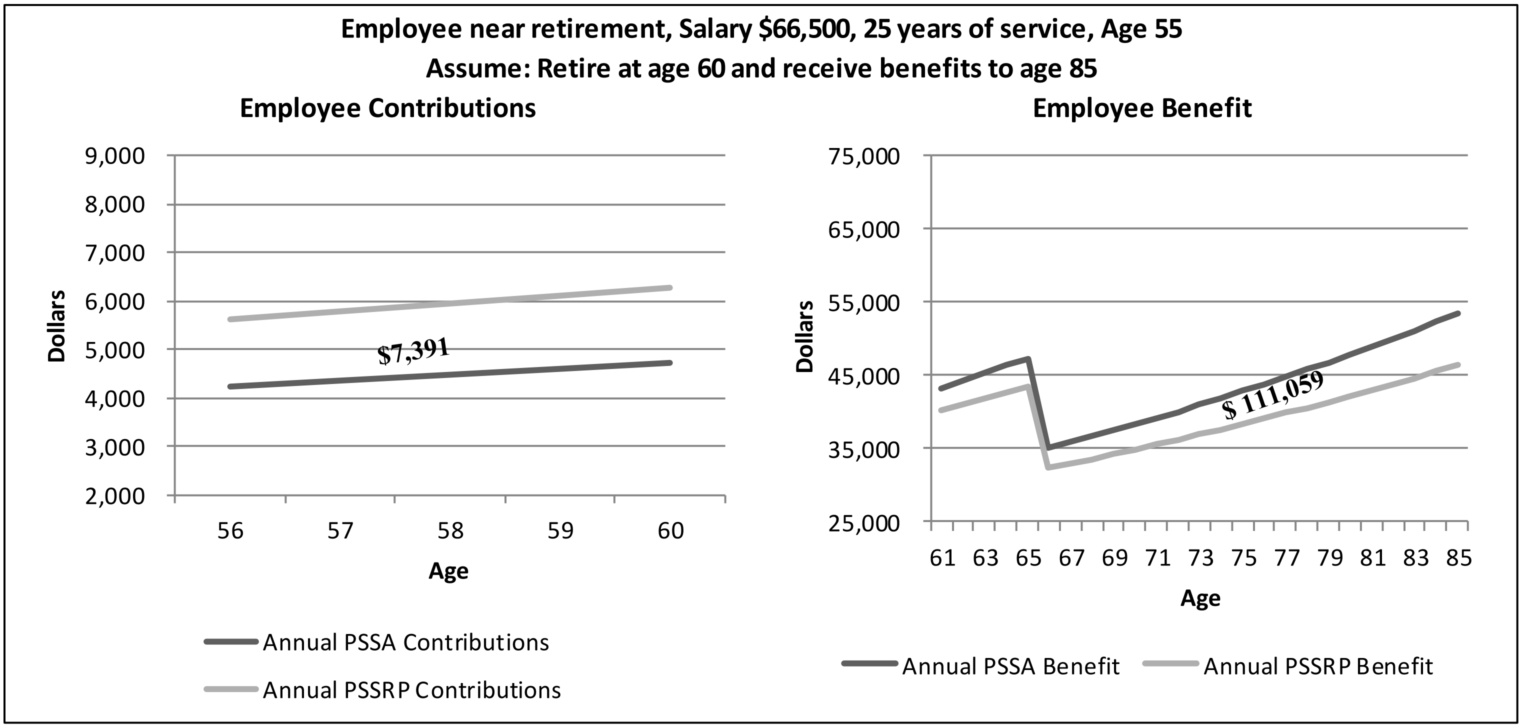
Exhibit 3.6 - Estimate of employee impact of PSSA/PSSRP plan changes

	Years of Service	PSSA (Previous Plan)		PSSRP (New Plan)		Decrease in total benefit accumulated if benefit paid to age 85	Increased contributions required during working life	Total employee impact of pension plan changes if benefit paid to age 85	Present Value of total employee impact to age 85
		Pension Benefit	Bridge Benefit	Pension Benefit	Bridge Benefit				
Employee near retirement salary $66,500, 25 years of service at start of new plan, 55 years old									
Employee Contributions in 2014		4,232		5,631					
Estimated Annual Benefit at Retirement at age 55 (2014)	25	19,377	7,413	19,377	7,413	**42,628**	**-**	**42,628**	**13,165**
Estimated Annual Benefit at Retirement at age 60 (2019)	30	31,352	11,963	29,394	10,886	**111,059**	**7,391**	**118,449**	**43,508**
Estimated Annual Benefit at Retirement at age 65 (2024)	35	41,891	-	40,515	-	**67,040**	**15,855**	**82,895**	**29,674**
Experienced employee salary $66,500, 15 years of service at start of new plan, 45 years old									
Employee Contributions in 2014		4,232		5,631					
Estimated Annual Benefit at Retirement at age 55 (2024)	25	25,434	9,705	20,533	7,318	**278,304**	**15,855**	**294,159**	**75,849**
Estimated Annual Benefit at Retirement at age 60 (2029)	30	41,123	15,691	34,541	11,857	**285,499**	**25,549**	**311,048**	**71,095**
Estimated Annual Benefit at Retirement at age 65 (2034)	35	54,947	-	56,642	-	**99,983**	**36,651**	**136,634**	**34,651**
New employee salary $40,000, 2 years of service at start of new plan, 32 years old									
Employee Contributions in 2014		2,384		3,083					
Estimated Annual Benefit at Retirement at age 55 (2037)	25	19,548	10,526	12,377	5,455	**386,091**	**22,010**	**408,101**	**53,386**
Estimated Annual Benefit at Retirement at age 60 (2042)	30	31,606	17,019	24,346	10,629	**307,271**	**28,899**	**336,170**	**40,095**
Estimated Annual Benefit at Retirement at age 65 (2047)	35	42,231	-	41,794	-	**44,671**	**36,788**	**81,459**	**16,332**

**See paragraph 3.20 and 3.21 for assumptions used in these calculations*

**See paragraph 3.21 for an explanation of bridge benefits*

Exhibit 3.7 - Estimate of employee impact of PSSA/PSSRP plan changes



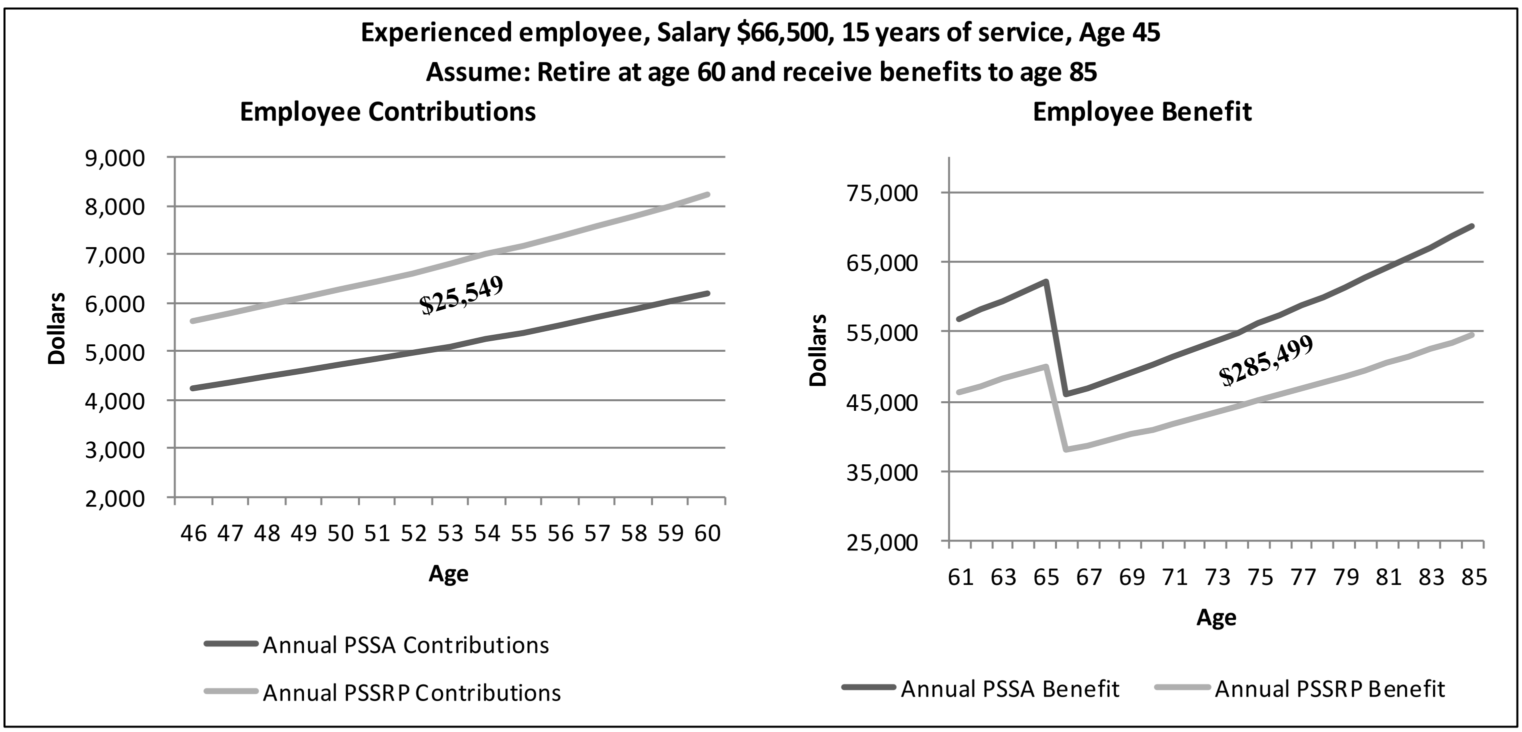


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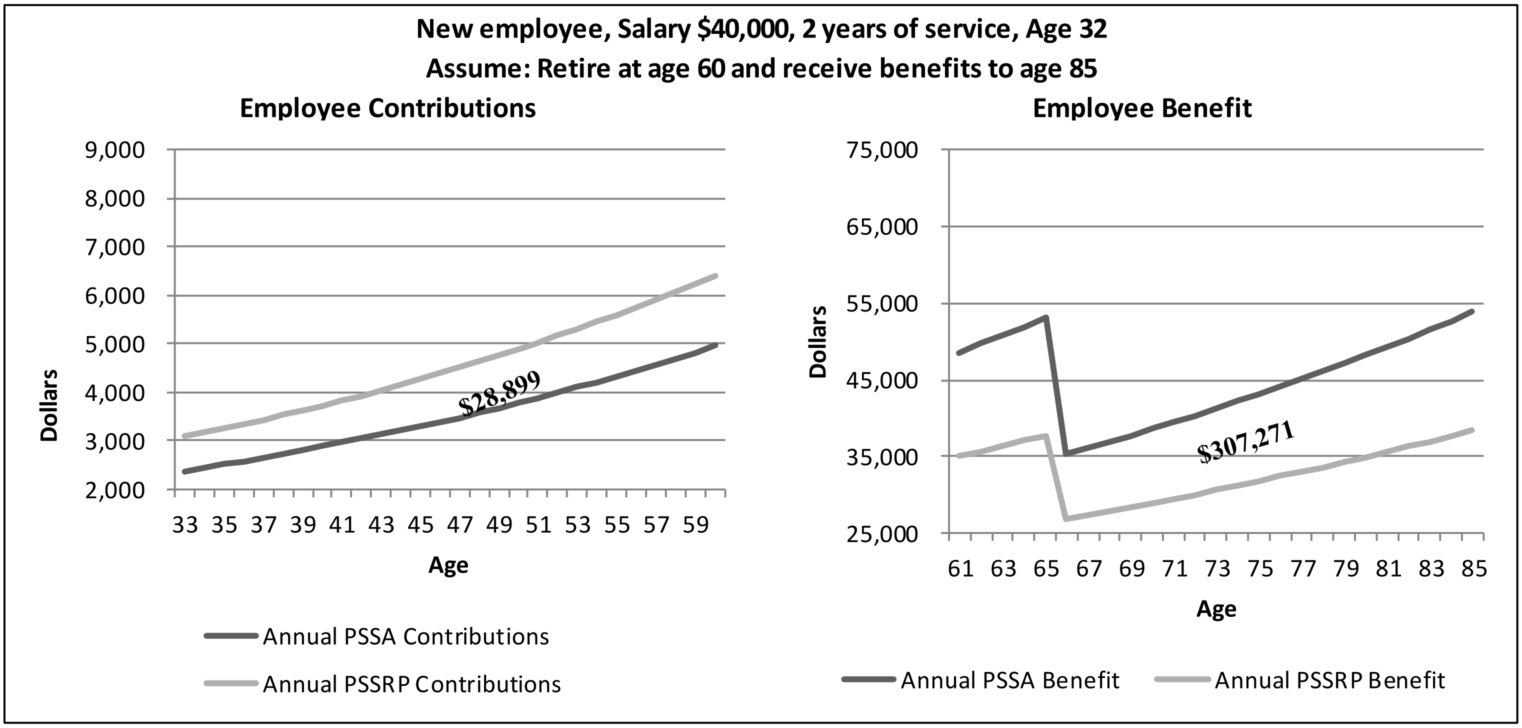
Exhibit 3.7 - Estimate of employee impact of PSSA/PSSRP plan changes (continued)



**See paragraph 3.20 and 3.21 for assumptions used in these calculations*

Significant assumptions

3.20 The following assumptions are used in calculating employee pension contribution amounts and pension benefits presented in Exhibits 3.6 and 3.7. These assumptions are used by the plan's actuary and include:

- From the funding valuation, annual salaries and yearly maximum pensionable earnings both are increased annually at rates of 2.75% until the age of retirement.
- From the funding valuation, inflation increases at an annual rate of 2.25% starting in 2014. Inflation under the PSSRP is calculated at 85.3% of inflation resulting in an effective inflation rate of 1.92%
- From the accounting valuation, a discount rate of 6.35% representing management's best estimate of future returns was used to calculate present values.

3.21 To provide consistency across employee scenarios in Exhibits 3.6 and 3.7, additional assumptions were made as follows:

- An annual salary of $40,000 is representative for a new employee.
- Annual salaries of $66,500 for the experienced employees are consistent with the average salary for active members of $65,523 as at April 1, 2013 which is used in the recent actuarial funding valuation.
- There is no interruption of employee service between January 1, 2014 and the retirement date.
- Employees live until the age of 85.
- Benefit amounts up to age 85 do not include any adjustments for amounts received by beneficiaries.
- The PSSRP calls for equal employee and employer contributions after 15 years. We have not made any adjustments to employee contribution rates as these rates are unknown at this time.
- We have assumed there to be no changes in benefits or contributions. However, as per the funding policy the PSSRP provides for potential reductions and increases in base benefits as well as temporary increases and decreases in employee contributions.
- Under both PSSA and PSSRP, if an employee is eligible for early retirement, a bridge benefit is paid in addition to their lifetime pension. The bridge benefit ceases to be paid when the employee reaches age 65 and is eligible for Canada Pension Plan benefits, or at their death, whichever is earlier. These bridge benefits have been shown separately in amounts presented in Exhibit 3.6 for information and included in employee impact totals.

3.22 In addition it should be noted the information in Exhibits 3.6 and 3.7 is difficult to calculate with exact accuracy. The PSSRP actuary produces 2000 economic scenarios in his testing for each of the next 20 years, based on a number of assumptions that may or may not occur; however, only one scenario of those 2000 tested will occur. It should also be noted current economic modelling only exists over the next 20 years, and in some cases estimates were necessary to extend beyond 20 years for purposes of calculating information for Exhibits 3.6 and 3.7. While certain complex assumptions are required in order to calculate this information, and assumptions may change as actual results are known, we believe there is value to presenting the estimates in Exhibits 3.6. and 3.7.

PSSRP pension plan changes have significant impacts on public servants

3.23 From review of the information in Exhibits 3.6 and 3.7, it is clear as a result of the plan changes, employees will pay more in contributions; receive lower benefits, work longer or a combination of all three of these outcomes. The amount of benefits expected to be earned at January 1, 2014 in the PSSA plan compared to the PSSRP plan in our example in Exhibit 3.6 for the relatively new employee retiring at 55 is a lifetime reduction in expected pension benefits of approximately $300,000 on a non-discounted basis.

3.24 In particular the pension plan changes are impacting the new and middle career employees the most, with employees near retirement being less affected by plan changes. The implementation of these plan changes allows those with the longest time to plan for retirement to react to their changed circumstances for retirement planning purposes.

3.25 Key factors decreasing employee future benefits under the new PSSRP include:

- a change from a best five year salary plan to an enhanced career average salary plan;
- a change from no retirement reduction factor at 60 to no retirement reduction factor now at 65; and
- an increase in the reduction factor calculation from 3% to 5%.

3.26 Also impacting employees is an increase in the contribution rates from 5.8% of earnings up to the Yearly Maximum Pensionable Earnings (YMPE) and 7.5% of earnings that exceed the YMPE, to 7.5% of earnings up to the YMPE and 10.7% of earnings that exceed the YMPE.

3.27 We noted that for employees with significant years of service the impact of the pension plan changes was reduced as the Province provided a guarantee that benefits earned prior to January 1, 2014 will never be reduced.

3.28 Information in Exhibit 3.6 has been presented on a discounted and non-discounted basis. Information presented on a discounted basis is shown as of January 1, 2014 using the 6.35% discount rate as per the January 1, 2014 accounting valuation. Given that information reported on annual employee pension benefits statements is presented on a non-discounted basis, we have also reported the non-discounted values, in Exhibit 3.6 as this would best reflect employee expectations of accrued pension benefits.

Pension Assets Rates of Return

3.29 The net interest component of the pension expense depends primarily on the rate of return earned on pension fund assets. These returns are volatile, as illustrated in Exhibit 3.8 which reports the rates of return for the New Brunswick Investment Management Corporation (NBIMC) since it was established in 1996 and diversified away from government bonds. The NBIMC manages the trust funds for the Province’s larger pension plans including the PSSA (now PSSRP) plan, the TPA plan and the Provincial Court Judges’ pension (Judges’) plans.

Exhibit 3.8 - NBIMC Rates of Return

NBIMC Rates of Return			
Year	**Percentage**	**Year**	**Percentage**
2014	13.56	2005	8.51
2013	9.08	2004	25.27
2012	5.00	2003	(6.95)
2011	10.42	2002	3.45
2010	19.94	2001	(5.23)
2009	(18.34)	2000	20.57
2008	0.79	1999	(0.62)
2007	8.68	1998	18.68
2006	15.87	1997	10.14
18 year annualized return			**7.15**

3.30 The returns earned by the NBIMC have ranged from a high of 25.27% in the year ended 31 March 2004 to a low of (18.34) % in the year ended 31 March 2009. Over the 18 fiscal years the annualized rate of return of the NBIMC has been 7.15%, which is above the 4.75% required for the PSSRP plan and above the 6.60% rate of return for the TPA plan currently required for funding purposes by the Province's independent actuary.

3.31 The rate of return for accounting purposes assumed by the Province on the significant plans in the 2013-14 consolidated financial statements was 6.35% and 6.50%. The accounting required for the Province's pension plans remains subject to estimates and the consolidated financial statements continue to remain exposed to volatility from many factors, including investment returns. Although NBIMC's rates of return have been volatile as shown in Exhibit 3.8, there has been reduced volatility experienced in the last four years.

Pension Accounting

3.32 Exhibit 3.9 provides the history of the Province's pension balance for accounting purposes and the important components involved in the calculation over the past ten years.

Exhibit 3.9 - Components of the Pension Balance for Accounting Purposes

Components of the Pension Balance for Accounting Purposes ($ millions)										
	2005	**2006**	**2007**	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**	**2014**
Estimated accrued benefit obligations	6,719.6	7,324.5	7,865.5	8,289.3	8,642.5	8,570.2	8,895.7	9,318.3	10,146.6	12,343.8
Value of plan assets	6,521.7	7,449.3	8,030.5	8,024.1	6,512.4	7,703.1	8,387.0	8,674.7	9,293.9	11,529.7
Pension position before accounting adjustments	197.9	(124.8)	(165.0)	265.2	2,130.1	867.1	508.7	643.6	852.7	814.1
Accounting adjustments	(41.2)	155.0	38.6	(509.9)	(2,340.3)	(1,063.7)	(728.6)	(903.1)	(1,002.2)	(814.7)
Pension balance for accounting purposes	156.7	30.2	(126.4)	(244.7)	(210.2)	(196.6)	(219.9)	(259.5)	(149.5)	(.6)

3.33 The pension balance for accounting purposes is calculated by comparing the estimated market value of plan assets to the actuarial estimate of accrued benefit obligations owing to present and future pensioners. From this difference an adjustment is made for accounting purposes. The purpose of the accounting adjustment is to reduce year to year pension expense volatility by allowing actual results achieved on plan assumptions to be reported over time and not all in one year. Exhibit 3.9 provides the details of these components of the pension balance.

3.34 Exhibit 3.9 shows that the Province's pension position before accounting adjustments improved in the year ended 31 March 2014 from $852.7 million to $814.1 million in 2014. The value of the estimated pension obligations before accounting adjustments exceeded the value of plan assets for the past eight years.

Accounting deferrals and adjustments are permitted under Public Sector Accounting Standards

3.35 The accounting adjustment row in Exhibit 3.9 is a critical part of pension accounting because it assumes a long term view, that the pension plan will be in existence over the long term and there will be volatility from year to year. Therefore, accounting standards permit for the smoothing of this volatility. Such adjustments for accounting purposes are allowed to be deferred and amortized into operating results in future years. Because the accounting adjustments are due to experience deferrals, the pension balance is in a negative liability position (presented in the Province's consolidated financial statements as a net pension liability) of $0.6 million at 31 March 2014.

3.36 As at 31 March 2014 the balance of accumulated experience adjustments (losses) for accounting purposes that were deferred and required to be amortized in future years totalled $814.7 million. Such deferral balances from experience adjustments are common in public sector pension accounting. While the cause of the experience adjustments results primarily from deviations to the assumed rate of return, it is a general indication that assumptions used in pension calculations did not match actual events. This accounting adjustment balance is also an indicator of the magnitude of the amount that must be recognized as an expense over future years.

Accounting for the Province's Shared Risk Pension Plans

3.37 As stated earlier in this chapter, during fiscal 2013-2014 New Brunswick's largest provincial pension plan converted to a Shared Risk Pension Plan model. This section will discuss the accounting considerations regarding this significant change. As background, we note that during fiscal 2012-2013 two pension plans converted to the new Shared Risk Pension Plan model: the pension plan for CUPE Employees of New Brunswick Hospitals (H-CUPE) and the pension plan for Certain Bargaining Employees of New Brunswick Hospitals (H-CBE). More information about the conversion of these specific plans can be found in our 2013 Report.

3.38 As part of the PSSA conversion process in fiscal 2013-2014 a number of changes were made to the previous PSSA pension plan including increasing the retirement age, introducing stronger reductions for early retirement, removing guaranteed indexing (now capped at 5%), introducing conditional indexing and establishing contributions at a higher level all to create a high probability that plan goals (sustainable, affordable, secure and transparent pensions) will be met. However, one of the key differences in this plan conversion compared to the prior year conversion of plans was that the Province had guaranteed that the benefits earned to the conversion date (January 1, 2014) by plan members would never be decreased.

Accounting for the Province's Shared Risk Pension Plans

3.39 The conversion to the Shared Risk Pension Plan model was a complex process for accounting purposes as the Public Sector Accounting Standard on pensions (*PS 3250 - Retirement Benefits*) does not fully address unique arrangements such as shared risk pension plans. PS 3250 does indicate that in some circumstances a benefit plan may include defined benefit and defined contribution elements, and PS 3250 also states that "because benefit plans are often complex, careful analysis and professional judgment are needed to determine whether the substance of particular plan makes it a defined benefit or a defined contribution plan."

Persuasive arguments for multiple accounting options

3.40 After reviewing the details of the shared risk pension plan arrangements and reviewing the accounting standards, we determined persuasive arguments could be made for both defined benefit and joint defined benefit accounting treatment based on the present accounting standards. It is important to note that this accounting classification is significant, as a joint defined benefit plan accounting treatment generally involves recording the employer share of the obligation and cost on the financial statements, whereas a defined benefit plan generally involves recording the entire plan obligation and cost in the financial statements. The PSSRP plan had been reported in the Province's past consolidated financial statements as a defined benefit pension plan prior to its conversion to a PSSRP structure.

3.41 Our assessment involved a complex evaluation of the plans' legislation and plan provisions. We caution that pension plan legislation and specific pension plan provisions may differ between pension plans (and different jurisdictions), and an assessment on a plan by plan basis is required to determine the appropriate accounting treatment of any pension plan conversion. Each pension plan must be assessed on its own merits. A high degree of professional judgment was exercised in the accounting model determination.

3.42 A significant question in the accounting analysis pertained to which party bears the risk in the pension arrangement: the employer or employee. A number of factors were considered in analyzing this question such as:

- level of variability in employer contribution;
- frequency of variability in employer contributions;
- likelihood of variability in employer contributions;
- whether separate accounts are maintained for each employee;
- whether employee benefits earned in the past may be reduced;
- communication to plan members;
- existence of guarantees; and
- presence of constructive or equitable obligations.

Province advocates defined benefit pension plan accounting

3.43 After considering all of these factors the Province's position was that the PSSRP plan should be accounted for as a defined benefit plan.

3.44 Highlighted in our audit work pertaining to this accounting decision were the following factors:

- the guarantee issued to members by the Province that there would be no reduction in benefits earned prior to January 1, 2014;
- the level of potential variability in employer contributions; and
- potentially large dollar impacts (and increased risk exposure) to the Province given the large size of this plan.

3.45 While factors existed to possibly consider a defined contribution accounting classification, they were not sufficiently persuasive. We agree with the overall plan classification as a defined benefit plan

Economic substance of the plans pre and post conversion

3.46 However, in our review of the plan details and structure it appeared as though a different defined benefit plan classification may be appropriate if the PSSRP was considered on a pre and post conversion basis. On a pre-conversion basis, the benefits earned are guaranteed by the Province and this leads more clearly to a defined benefit accounting conclusion. On a post-conversion basis the economic substance of the plan has changed somewhat as the benefits are not guaranteed post-conversion. Therefore, on a conceptual level, there is an argument for considering there are two plans, each deserving of their own consideration and classification.

Joint defined benefit plan possibility for post-conversion service

3.47 It is possible that upon further review it may be determined that the PSSRP has more similarities to a joint defined benefit plan as the plan matures. In a joint defined benefit plan the risks are shared between the government and the plan participants on an equitable (but not necessarily even or identical) basis and the funding contributions are shared mutually between the government and the plan members. In future, as more non-guaranteed post-conversion service is rendered the government will likely retain less residual risks and the risks will become more evenly shared post conversion. Joint defined benefit accounting may then be a more appropriate basis to record the post-conversion services, costs and obligations.

3.48 Under joint defined benefit plan accounting the Province would only record the portion of the liability, cost etc. that relates to the portion of the costs and risks the employer (the Province) assumes (possibly 50% or some other appropriate percentage). This would likely, over time, cause a significantly different result in the Province's audited financial statements as more of this post-conversion service accumulates in large amounts.

3.49 We believe this matter should be studied further. In the near future the majority of the plan liability is derived from pre-conversion service. There is little post-conversion liability until more significant employee service time has elapsed under the post-conversion plan. However, as time passes the amount of post-conversion service will grow, and if the plan classification were to change to joint defined benefit, a significant adjustment may result for accounting purposes.

Defined benefit accounting accepted for PSSRP

3.50 However, for the year ended 31 March 2014, the Province's view is that the appropriate classification of the PSSRP, given the guarantee arrangement and other factors, is as a defined benefit plan. We agreed with this conclusion at this time given the limited amount of post-conversion service, but recommended this decision be reviewed to investigate this accounting alternative in future.

Future accounting standards changes may impact accounting decision

3.51 It is important to note accounting standards are evolving and there have been changes in pension accounting standards internationally. In addition, pension accounting standards in Canada may also change to better reflect the emerging structures of new pension plan models. We will continue to monitor accounting standards as they evolve, and our conclusion on the appropriate accounting treatment for the PSSRP, H-CUPE and H-CBE plans may change in future depending on the changes in accounting standards.

3.52 Given the Province's announced intention to convert more pension plans to shared risk pension plans we believe the question of appropriate accounting treatment will continue to be an important issue in future audits.

Chapter 4
Matters Arising from our Audit of the Financial Statements of the Province

Contents

Matters Arising from our Audit of the Financial Statements of the Province

Introduction

4.1 On July 17, 2014 the Auditor General signed an unqualified audit opinion on the consolidated financial statements of the Province of New Brunswick.

4.2 This was a significant milestone for our Office and the Province as it was the earliest known completion date in recent years for New Brunswick's public accounts audit. We are grateful for the dedication and commitment of our staff, the Office of the Comptroller and other government employees in their collaboration and support to achieve this goal. We hope to continue to achieve similar early completion dates in future years.

4.3 The opinion signed July 17, 2014 indicates the Province's consolidated financial statements are fairly presented in accordance with Canadian public sector accounting standards.

4.4 To reach an opinion on the consolidated financial statements of the Province, we carry out audit work on the major programs and activities in departments. In addition, we audit major revenue items and a sample of expenditures chosen from departments. We also examine internal controls of significant computerized systems.

Audit Findings

4.5 In almost every audit, there are audit findings to be discussed with management. While significant, the findings from our March 31, 2014 audit are not sufficiently large in dollar or qualitative terms to affect our opinion on the consolidated financial statements. It is our practice to report these matters to senior officials of the departments concerned, and to ask for a response. Our significant findings and recommendations from the audit of the Province's consolidated financial statements with departmental responses are presented in this chapter.

4.6 It should be noted though that not all findings are included in the Report, because in some instances we do not consider them to be of sufficient importance to bring to the attention of the Legislative Assembly, or because public attention to internal control weaknesses, before they are corrected, could possibly result in loss of government assets. For further background on our audit objectives refer to Appendix I.

4.7 We had several findings from the March 31, 2014 audit of the Province's consolidated financial statements. We review the findings identified to determine which findings from our work are significant. When considering which findings are significant we assess:

- dollar magnitude of the item;
- the risk the finding could result in a large loss or error in future;
- the number of instances the finding has occurred;
- if the finding has occurred in multiple departments;
- if the finding was reported in a prior year; and
- if we believe the finding is overall significant in nature.

Highlights and Recurring Themes

4.8 Highlights and recurring themes of our significant findings are presented in Exhibit 4.1.

4.9 We are concerned at the trend of findings not being corrected in advance of the next year's audit cycle. Exhibit 4.1 presents the recurring findings in shaded boxes. We have adopted a new reporting format for this chapter to assist in highlighting repeat findings for further review and action.

Exhibit 4.1 -Highlights and Recurring Themes

Theme	Finding	Finding addressed to	Concern in this area also noted in 2013 AG Report	Concern in this area also noted in 2012 AG Report	Paragraph Number
Accounting Concerns	Liability for contaminated sites – new PSAB standard for 2015	OOC[1]	Yes	No	4.68
	Proper and complete accounting for school raised funds	OOC[1]/EECD[3]	No	No	4.69
	Pension accounting – shared risk pension plans	OOC[1]	Partial	No	4.73
	Classification of accounts in the consolidated financial statements	OOC[1]	No	No	4.77
	Grants/government transfers – need for accounting analysis	OOC[1]	Yes	No	4.79
	Tangible capital assets (TCA) – communication of tangible capital asset policy and asset impairment assessment	OOC[1]/ DTI[2]	No	Partial	4.78
	Property tax revenue - municipal suspense account reconciliations	Finance	Yes	Yes	4.81
	Netting of property tax revenue	Finance	No	No	4.82
	Support for and review of changes to property tax assessment values	Service New Brunswick	Partial	No	4.83
Governance/ Oversight Concerns	Need for an audit committee	Finance	Yes	Yes	4.70
	Need for an internal audit plan	OOC[1]	No	No	4.71
	Need to align Administration Manual Policy AD6402 – Approval of Payments	OOC[1]/ NBISA[7]	Yes	No	4.74
	Need to complete purchase card policy	OOC[1]	Yes	No	4.72

Continued on following page

Exhibit 4.1 -Highlights and Recurring Themes (continued)

Theme	Finding	Finding addressed to	Concern in this area also noted in 2013 AG Report	Concern in this area also noted in 2012 AG Report	Paragraph Number
Accounting/ Documentation Concerns With Estimates	Need to review allowance for doubtful accounts – loans and accounts receivable	OOC[1]/ SD[4]/ PETL[5] / AAF[6] / Justice/	Yes	Partial	4.75
	Need to update estimate of federal tax revenues	Finance	No	No	4.76
	Write off of accounts and loans receivable policy	OOC[1]	No	No	4.80

Shaded findings indicate a concern in this area was also noted in the 2013 or 2012 AG Reports
[1]*Office of the Comptroller, Department of Finance*
[2]*Department of Transportation & Infrastructure*
[3]*Department of Education and Early Childhood Development*
[4]*Department of Social Developments*
[5]*Department of Post-Secondary Education, Training and Labor*
[6]*Department of Agriculture, Aquaculture and Fisheries*
[7]*New Brunswick Internal Service Agency*

4.10 In general, departments' responses indicated they agreed with our recommendations and they intend to address our concerns in the coming year.

4.11 While we have not noted any significant fraud, theft or error as discussed later in Appendix II, the existence of the findings noted in Exhibit 4.1 increases the risk of loss or mistake in the Province's consolidated financial statements. These items should be addressed prior to the next audit cycle.

Details of Significant Findings

4.12 Our detailed observations, recommendations and departmental responses to our full list of significant findings are presented in Appendix III. Summarized comments pertaining to the key themes of our audit findings are presented in the following paragraphs.

Additional Discussion

Accounting concerns

4.13 During our audit of the Province's financial statements we noted nine concerns pertaining to accounting, six of which were previously reported in either our 2013 or 2012 Annual Reports. In general, the findings regarding accounting related mostly to appropriate application of accounting standards, accounting errors or other concerns.

4.14 Accounting standards continue to evolve as new standards are introduced (e.g. environmental liabilities) and as existing standards are applied to new situations (e.g. shared risk pension plans - refer to Chapter 3 for further comments). Proper application of accounting standards is important to ensure financial results are fairly presented.

4.15 In recent years accounting standards issues have involved complex questions and judgments, as well as significant dollar transactions and balances. We expect this trend to persist as accounting standards continue to change. We continue to encourage the Office of the Comptroller and Department of Finance to be proactive in addressing accounting standards changes to allow for timely resolution of accounting questions and sufficient time for appropriate analysis. Also, appropriate expert advice to address complex technical matters should continue to be obtained as needed.

4.16 Other accounting weaknesses noted relate to accounting errors or other accounting concerns. Repeat findings of this nature such as reconciliation of municipal property tax revenue and other accounting issues are particularly concerning. These items involve significant transaction streams and could, if not addressed, cause large adjustments in the Province's consolidated financial statements during the audit process.

Governance/ oversight concerns

4.17 During the Province's financial statement audit, we also noted four findings related to governance or oversight weaknesses. Three of these findings were previously reported in either our 2013 or 2012 Annual Reports. One of these findings regarding a lack of an audit committee has been present all of the last three years (2014, 2013, and 2012). An audit committee would bring increased scrutiny to provincial financial and risk management practices, as well as provide increased discipline and structure to management reporting, which would in turn reinforce accountabilities.

4.18 Our oversight/governance findings represent foundational weaknesses in the Province's internal control and risk management practices. Appropriate committee oversight, internal audit plans and completing and approving policies which govern millions of dollars in spending are all important parts to strengthening the Province's internal control and risk management environment. We will revisit these audit areas again next year.

Accounting/ documentation concerns with estimates

4.19 In addition, we noted three findings related to accounting/documentation concerns with estimates. One of these findings (estimating loans and accounts receivable allowances for doubtful accounts), was a repeat finding from our prior year reports. Estimates involve the application of judgment on matters where the outcome is unknown. In the cases of our findings, the amounts involved in the estimate process are significant.

4.20 Auditing standards have introduced increasing rigor for auditors to challenge significant management estimates and underlying assumptions including a review of prior year’s estimates to assist in determining estimate accuracy.

4.21 As the outcomes of estimates are unknown, and significant judgment is being applied, documentation, support and approval for these amounts are important parts of our audit process.

Information Technology Findings

Auditing the Province's systems and information technology

4.22 In order to express an opinion on the Province's financial statements, we document controls and test transactions processed by significant financial IT systems. Some of this work is performed on a cyclical basis. We also document the controls associated with the Province's overall IT infrastructure. Exhibit 4.2 lists IT systems we examined in the past year:

Exhibit 4.2 - IT systems examined in the past year

Department	Audit
Education and Early Childhood Development (EECD)	Teachers' Payroll
Finance	Property Tax System (Ptax)
New Brunswick Internal Services Agency (NBISA)	HRIS Payroll System
	Oracle Input System (IPM)
	IT Infrastructure
Office of the Comptroller (OOC)	Oracle Financials
Service New Brunswick (SNB)	Property Tax Assessment System
Social Development (SD)	Long-term Care System-NBFamilies
	Social Assistance Payment System - NBCase

Key Themes

4.23 We are not publishing the details of all of our IT system work given the technical nature of many of our findings, and as noted previously in this chapter, the risk of possible loss of government assets if the details of such findings are reported. Instead, we are summarizing our findings into key themes by the responsible department. We are reporting this information in Exhibit 4.3.

Exhibit 4.3 -Information Technology Findings – Key Themes

Theme	Finding	Finding addressed to
Segregation of Duties	Developers' access to production	OOC (Oracle)
	Approval of Purchase Cards	EECD
System Replacement	Teachers' payroll system	EECD
	Property tax system	Finance (PTax)
IT Security	Excessive permissions	NBISA (HRIS), OOC (Oracle), NBISA (IT Infrastructure)
	Disabling access	OOC, NBISA (IT Infrastructure), SNB
	Encryption of data	NBISA (IT Infrastructure)
	Monitoring – Administrators, Third-party service	OOC (Oracle), SNB, NBISA (IT Infrastructure)
	Patch management	OOC (Oracle), NBISA (IT Infrastructure)
	Firewall rules	NBISA (IT Infrastructure)
	Access controls	NBISA (IT Infrastructure), SNB
	Management of network access	NBISA (IT Infrastructure)
Data Integrity/Accuracy/ Completeness	Electronic Transfer of Data	NBISA (HRIS)
	Departmental payroll reconciliations	NBISA (HRIS)
	Monitoring Exception reports	OOC (Oracle)
	Quality of assessment data	SNB
	Reconciliation of assessment system to property tax system	SNB
Disaster Recovery / Backup of Key Staff	Disaster recovery plan	OOC
	Backup of payroll personnel	EECD
Non-compliance with policies/standards/guidelines	Password standards	SNB, NBISA (IT Infrastructure)
	Assessment re-inspection cycle	SNB
	Annual client reviews	SD (NBFamilies)
	Adult residential facility inspection and licensing	SD (NBFamilies)
	Financial assessments/client contributions	SD (NBFamilies)
Documentation Deficiencies	Payroll documentation	NBISA (HRIS)
	Expired funding application for intervention services	SD (NBFamilies)
	Contracts with service providers not available	SD (NBFamilies)
Approvals	Pre-inspection road reviews for property assessments	SNB
	Completing delegation forms	EECD, SD
	Documenting approval	Finance (Ptax), SD (NBCase), NBISA (IPM)

4.24 We are not aware of any loss of government assets or errors which resulted from the findings noted in Exhibit 4.3, however, we are concerned for the potential for future loss of assets or error. Given the findings pertaining to IT security as noted in Exhibit 4.3 we are also concerned for the potential of loss of confidentiality and privacy inherent in the above noted findings if they remain uncorrected.

4.25 It should be noted this work was performed with a focus on the financial statement audit impact. Risks arising as a result of operational or confidentiality/privacy concerns are noted where observed but were not the main focus of our work.

Additional Discussion

4.26 Given the significance of some of the findings and the fact we have similar findings across multiple departments, we will discuss some of the findings outlined in Exhibit 4.3 in more detail.

Segregation of Duties

4.27 We noted two findings relating to a lack of segregation of duties. One finding relates to the Oracle application which we reported in the prior year. This recommendation was partially implemented by the OOC with the expectation for full implementation in 2015. The second finding relates to the approval of purchase card transactions in the department of EECD. We found five cases in our 22 item sample of EECD purchase card transactions where the cardholders provided spending authority on their own transactions. Proper segregation of duties is necessary to reduce the risk of fraud and error in the accounting records.

System Replacement

4.28 Similar to prior year, we have findings relating to outdated IT systems. We found two systems need to be replaced or modernized.

4.29 When we audited the teachers’ payroll system, we found limited progress on system replacement in the past year. We did note approval was obtained to proceed with a Business Study with the intention of going forward with a new Human Resource Management solution for Part II employees (e.g. teachers). Replacing the teachers’ payroll system is critical as access security is extremely weak, support is provided by a single contractor with no backup and the system runs on old, out-dated hardware. The system is over 20 years old and is at a risk of failure. The EECD did obtain a risk assessment to identify the risks associated with this system. We noted, however, the risks identified, although significant, were unable to be mitigated without developing a new system. We recommended a replacement solution be implemented as soon as possible.

4.30 In the case of the Department of Finance Property Tax system, the Department informed us implementation of phase I of this system is on target for the 2015 fiscal year.

IT Security - Excessive Permissions

4.31 We noted findings in three of our audits relating to excessive system access. We found cases where:

- an informal process exists for tracking, documenting and approving the use of the administrator account;
- an excessive number of user accounts exist with certain administrator privileges; and
- IT support had functional access to the system and appropriate monitoring controls were not in place to reduce this risk.

4.32 Allowing users excessive access to systems and data increases the risk of individuals gaining unauthorized access to financial information or system functionality which could result in fraud or error in the accounting records.

IT Security - Disabling Access

4.33 We noted findings in three of our audits relating to the process of disabling users' system access. We found cases where:

- resigned/terminated employees users' access was not removed/disabled in a timely manner;
- users' access was not disabled within 90 days of inactivity as required by policy; and
- users' access was not confirmed on an annual basis to ensure the access was still appropriate.

4.34 Timely disabling of user accounts, along with an annual review of user access assignments reduces the risk of unauthorized transactions being executed by terminated or existing employees, loss or corruption of data and exposure of confidential corporate information.

IT Security - Encryption of Data

4.35 We noted findings relating to encryption of hardware and data. Having appropriate encryption controls in place helps safeguard information and reduces the risk of a breach of confidentiality in the event of unauthorized access of data/hardware or theft.

IT Security – Monitoring of Service Providers and Administrators

4.36 In two audits, we had findings related to the monitoring of outsourced third-party services. The lack of appropriate monitoring controls increases the risk that processes performed by third parties are not performed in accordance with expectations.

4.37 We also noted in two audits a lack of monitoring of IT support/database administrator’s activity. These administrators/individuals have powerful system access. Proper monitoring controls are required to reduce the risk of unauthorized changes/updates to significant database tables.

IT Security –Patch Management

4.38 In two audits, we noted weaknesses in the patch management strategy used to ensure software and operating systems are running current versions. Failure to have an appropriate patching strategy increases the risk software vulnerabilities could be exploited by outside parties, which could result in loss of information and impact the stability of applications.

IT Security - Firewall Rules

4.39 During our audit, we noted two observations relating to firewall rules (the firewall is designed to filter system traffic to ensure system access is appropriate and authorized). One observation related to the approval of changes to the firewall rules and the other related to enabling firewall rules and logging activity. Failure to have proper firewall controls in place could negatively impact the confidentiality, integrity and availability of network resources and financial information.

IT Security - Access Controls

4.40 We had findings in two audits related to access controls. One finding related to the system owner not approving user access. The other related to changing the default passwords for database accounts. Proper system access controls are required so only authorized employees obtain access to the system.

Data Integrity/Accuracy / Completeness

4.41 We had two findings relating to the transfer of information between systems. In both cases, we recommended controls be implemented to ensure the transfer of information between the systems is complete and accurate.

4.42 We had findings relating to accuracy of assessment information recorded in SNB's property tax assessment system. We noted the work of assessors is not reviewed. This lack of review related to both calculating the property assessment values and the input of information into the assessment system. We were told a sample of this information is reviewed by regional managers. As the review was not documented, we found no evidence of this review. Verifying the accuracy of assessment information is required to reduce the risk of inaccurate property assessment values which could result in the over/understatement of provincial revenue.

4.43 We also had findings relating to the timeliness of payroll reconciliations and the monitoring of exception reports. Control procedures relating to verifying the accuracy of data such as preparing reconciliations and reviewing reports help reduce the risk of inaccurate and incomplete financial information.

Disaster Recovery and Backup Support

4.44 In our audit of the Oracle Financials system, we noted the disaster recovery and business continuity plans were out-of-date. The OOC is in the process of updating these plans, but this work is not yet complete.

4.45 We also noted a lack of backup payroll personnel for the EECD teachers' payroll system. The Department indicated this weakness is a direct result of having an out-dated payroll system which prohibits sharing of district staff. Having trained backup of payroll personnel is necessary to reduce the risk of payroll not being processed in a timely manner or errors occurring in processing due to inexperienced individuals preparing payroll during unplanned absences.

Non-compliance with policies /standards /guidelines

4.46 In our work, we noted six cases where departments failed to comply with departmental policies/standards or guidelines.

4.47 In our audit of SNB assessments, we noted the Agency had not visually inspected 193 of 842 neighborhoods in more than ten years. SNB aims to perform a visual inspection on every property in the Province within a ten-year timeframe. Completing re-inspections within the ten-year timeframe helps reduce the risk of inaccurate property assessments which would result in provincial tax revenue being over or understated.

4.48 We found three areas of non-compliance in our audit of the NBFamilies system. We found seven of ten cases examined where clients' annual case reviews were not up-to-date. We found one of six cases examined where the license for an adult residential facility had expired and was not renewed in the time frame required by policy. Finally, we found three of 11 cases examined where client financial assessments were not updated as required by departmental policy. Of these three cases, one resulted in an incorrect client contribution. Not complying with departmental policy increases the risk of SD making ineligible or inaccurate payments.

4.49 During our testing of NBCase payments in SD, we found no evidence of spending authority being exercised on payments from the system. This documentation is required to comply with the Province's approval of payments policy.

Documentation Deficiencies

4.50 In two audits, we noted documentation deficiencies. In the NBISA (HRIS) audit, we noted documentation weaknesses relating to obtaining evidence to support employees' date of birth, completing standardized checklists, and documenting errors noted in discrepancy reports. Having proper documentation on file provides evidence internal controls are operating effectively and helps to reduce errors in financial data.

4.51 In the NBFamilies audit, we found one item in two cases where the funding application for a payment had expired at the time of the payment. We also found one item in six cases examined where a contract with a service provider and/or an agreement showing the service provider was authorized to receive the payment was not available. Not having up-to-date funding agreements or signed contracts on file increases the risk of ineligible and/or incorrect payments.

Approvals –Delegating Authority

4.52 In two departments, we found issues in the delegation of authority for the approval of payments. In SD, we found one case where a spending delegation form was not present to authorize the person approving the payment. In the annual confirmation of spending authority access, we found one case where SD incorrectly confirmed approval spending limits. Properly delegating spending authority reduces the risk of unauthorized or inappropriate payments.

4.53 In EECD, we found one school district used the same form to delegate two different types of approval without identifying the types of approval being delegated. The functions associated with each type of approval are different and by not distinguishing between them, the risk of inappropriate approval of payments increases.

Approvals – Documenting Approval

4.54 In SNB we noted regional managers are not always documenting their review and approval of the pre-inspection road reviews which support property assessment values. Documenting approval of the road reviews help ensure the accuracy of assessment data.

4.55 In the property tax system audit, we noted the approval of refunds was not always noted on the supporting documentation. This evidence is necessary to ensure all refunds are authorized and valid.

4.56 In the NBISA (IPM) audit, we noted formal documented approval was not required to move a system/application change into production (to make a change to the system currently in use). This approval is necessary to reduce the risk of unauthorized or untested changes being put into production.

Appendix I - Audit Objectives

4.57 Our examination of the matters included in this chapter of our Report was performed in accordance with Canadian generally accepted auditing standards, including such tests and other procedures as we considered necessary in the circumstances. The matters reported should not be used as a basis for drawing conclusions as to compliance or non-compliance with respect to matters not reported.

4.58 We obtain reasonable assurance on the financial statement figures because it would not be cost effective to obtain absolute assurance - our auditors cannot test every transaction.

4.59 By applying audit procedures to test the accuracy or reasonableness of the figures appearing in the financial statements, we achieve our desired level of assurance. We use audit procedures such as tracing samples of transactions to supporting documents, testing the effectiveness of certain internal controls, confirming year-end balances with third parties and reviewing the reasonableness of estimates.

4.60 Because of the limited objectives of this type of audit work, it may not identify matters which might come to light during a more extensive or special examination. However, it often reveals deficiencies or lines of enquiry which we might choose to pursue in future audit work.

Responsibilities Pertaining to the Audit Process

4.61 The government is responsible for the preparation and the content of the Province's financial statements. The Statement of Responsibility at the front of Volume 1 of Public Accounts is signed by the Minister of Finance on behalf of the government. The Comptroller is responsible for preparing the financial statements in accordance with Canadian public sector accounting standards. When preparing the financial statements, the government must make significant estimates, as not all information is available or determinable at the time of finalizing the statements. Examples of areas where management has made estimates in the financial statements are: provision for loss on loans and accounts receivable, contingencies, employee future benefits, environmental liabilities, tax revenue reassessments from prior years, tangible capital assets amortization rates and timing of rehabilitation work completed under public private partnership road contracts (which may not reflect when work is actually completed by the contractors and may impact classification of payments as prepaid expenses, accrued expenditures or tangible capital assets).

4.62 Our Office is responsible for auditing the financial statements. An audit provides reasonable, but not absolute, assurance that the Province's financial statements are free of material misstatement. Material misstatement refers to an item or group of items that, if omitted or misstated, would alter the decisions of reasonably knowledgeable financial statement users. The tolerable level of error or misstatement is a matter of judgment.

Appendix II - Loss through Fraud, Default or Mistake

4.63 Section 17(2) of the *Auditor General Act* indicates that the Auditor General may report to the Legislative Assembly cases where fraud or illegal activity has been discovered.

4.64 During the course of our work we became aware of the following losses. Our work is not intended to identify all instances where losses may have occurred so it would be inappropriate to conclude that all losses have been identified.

Department of Education and Early Childhood Development Missing netbook and re-keying of a school	$ 2,276
Department Energy and Mines Missing Phone	$ 600
Department of Justice and Attorney General Missing cash	$ 341
Department of Natural Resources Missing equipment from various regions	$ 5,595
Department of Post-Secondary Education, Training & Labour Alleged Fraudulent Claim	$6,664
Department of Transportation and Infrastructure Missing equipment and diesel fuel	$ 7,541

4.65 Losses reported by our Office only include incidents where there is no evidence of break and enter, fire, or vandalism.

4.66 The Province reports in Volume 2 of the Public Accounts the amount of lost tangible public assets (other than inventory shortages).

4.67 In 2014, the Province reported lost tangible public assets in the amount of $23,017 compared to a loss of $27,954 reported in 2013.

Appendix III - Significant Findings

4.68	**Liability for contaminated sites – new PSAB standard for 2015**

Public Sector Accounting Standard PS3260 – Liability for Contaminated Sites effective for the period ending March 31, 2015 requires the Province to account for and report the expected costs to remediate contaminated sites. During our audit, we noted departments provided lists of known contaminated sites to the Office of the Comptroller. However, we were concerned to note that a process had not yet been developed for estimating liabilities. PS3260 indicates a liability for remediation of contaminated sites should be recognized when, as at the financial reporting date: an environmental standard exists; contamination exceeds the environmental standard; the government is directly responsible or accepts responsibility; it is expected that future economic benefits will be given up; and a reasonable estimate of the amount can be made.

As the adoption of the new accounting standard will require additional audit work to be performed, we request this work be completed no later than December 2014.

Recommendations	**Comments from Management**
We recommend the Office of the Comptroller prepare an analysis of the new standard and its impact on the financial statements of the Province. **We recommend the Office of the Comptroller ensure a list of contaminated sites is prepared including estimated liability amounts to allow for evaluation and audit on the consolidated financial statements. A formal plan should be in place including goals and timelines to permit completion of this work ideally no later than December 2014.**	*The Officer of the Comptroller will continue to prepare for the implementation of this standard effective for the fiscal period ending March 31, 2015.*

4.69	Proper and complete accounting for school raised funds

Each year millions of dollars are collected for school raised funds. During our audit work we noted the Province is accountable for school raised funds, however, from our work in three school districts we were told school raised funds are not recorded in the Province's consolidated financial statements.

Recommendation	Comments from Management
We recommend the Office of the Comptroller and Department of Education and Early Childhood Development ensure proper and complete accounting for all revenue related to school raised funds and ensure consistent policies and procedures for school raised funds are in place for all school districts.	*The Office of the Comptroller will work with the Department of Education and Early Childhood Development to ensure the proper and complete accounting for school raised funds. Where possible, we will recommend consistent policies and procedures be used.*

4.70	Need for an audit committee

Canadian auditing standards require auditors to communicate to those charged with governance of an entity (e.g. audit committees or boards of directors) certain matters that may assist them in their governance roles and in overseeing management's financial reporting and disclosure processes. Matters that require communication if present include but are not limited to:

- Significant audit adjustments and/or deficiencies in financial statement disclosures;
- Significant weaknesses in internal control;
- Disagreements with management;
- Significant issues discussed, or subject to correspondence, with management;
- Significant difficulties encountered during the audit; and
- Fraud and illegal acts.

As noted in prior years, the Province of New Brunswick has no formal audit committee.

Recommendation	Comments from Management
We again recommend the Department of Finance establish an audit committee for the Province of New Brunswick.	*The Office of the Comptroller recognizes the important role an audit committee serves. We will continue to work with other divisions within the department to establish an audit committee.*

4.71	**Need for an internal audit plan**
We noted the Audit and Consulting Services Branch of the Office of the Comptroller did not have a formal internal audit work plan completed for the 2013-2014 year. Having an effective internal audit plan helps facilitate alignment of internal audit initiatives and assists management and those charged with governance (audit committee) in their role of minimizing exposure to the Province.	
Recommendation	**Comments from Management**
We recommend, on an annual basis, the Audit and Consulting Services branch of the Office of the Comptroller develop an internal audit plan and communicate the internal audit plan to the audit committee. The internal audit plan should detail the nature and timing of the projects to be completed in the upcoming year.	*The Internal Audit and Consulting Services branch of the Office of the Comptroller recognizes the importance of an internal audit plan and is in the process of developing a plan for the 2015-2016 fiscal year. Pending an audit committee being established, this plan will be communicated through the Comptroller to the Deputy Minister of Finance. The terms of reference which establish an audit committee will determine what reporting is made to that committee.*

4.72	**Need to complete purchase card policy**
Again this year, we noted the Province does not have a policy in place regarding the use of purchase cards. Annual purchase card transactions are over $21 million. A draft policy from 2005 does exist; however, it has never been finalized. In our work, we noted certain cardholders had exercised spending authority over their own transactions. This increases the risk of inappropriate purchase card use and misappropriation of funds.	
Recommendation	**Comments from Management**
We again recommend the Office of the Comptroller finalize the purchase card policy in fiscal 2015.	*The Office of the Comptroller is working in with the New Brunswick Internal Services Agency and the Department of Government Services to finalize the purchase card policy. The target completion date is 2015.*

4.73	Pension Accounting – Shared risk pension plans

As changes to the Province's pension plans are ongoing it is important to evaluate the accounting options on a regular basis.

Consideration should be made on a go-forward basis as to whether post-conversion benefits of the Public Service Shared Risk Plan (PSSRP), the pension plan for CUPE Employees of New Brunswick Hospitals (H-CUPE) and the pension plan for Certain Bargaining Employees of New Brunswick Hospitals (H-CBE) should be accounted for as Joint Defined Benefit plans. Accounting for the plans as a Joint Defined Benefit plan could have significant impacts going forward as the employer would only recognize the portion of the service cost relating to the portion of costs and risks that the employer is obligated. In future years, this would also result in a materially lower obligation for the employer related to the post-conversion service.

The PSSRP Accrued Benefit Obligation ("ABO") was measured on conversion assuming indexing at 100%. While this is a conservative estimate, it is unlikely full indexing will be provided. Also considering the secondary risk management goal, as stated in the Office of the Comptroller's position paper, over a 20 year period, on average the ancillary adjustments will exceed 75% of their potential value (i.e. meet or exceed 75% of the increase in consumer price index in the case of indexation) we would question if actual indexing should be estimated in the calculation in the range of 100% and 75%. In our view, using an indexation estimate based on expected level of indexation to be provided would be a more appropriate measure of the ABO.

The UP94 mortality table using partially enhanced projection Scale AA was used in the valuation of the PSSA/PSSRP in the current year. This is an outdated actuary table which is based on US experience prior to 1994. Despite the table was adjusted to reflect the 'enhanced projection scale' which was developed by the NB Pension Task Force and adopted by the Board of Trustees for the PSSRP, consideration should be given to either revising this assumption or using the new Canadian tables on a go-forward basis. Reasoning for selection of a set of tables should be documented.

As changes to the structure of the Teachers' Pension Plan are expected, the Office of the Comptroller should engage appropriate expert pension accounting resources to evaluate and select accounting options. Ideally, this work should be completed no later than December 2014.

Recommendations	Comments from Management
We recommend the Office of the Comptroller evaluate on an annual basis the classification of the PSSRP, H-CUPE and H-CBE, which considers changes in accounting standards and has clear documentation indicating support for the current year classification of these plans.	*The Office of the Comptroller recognizes the importance of proper accounting for pension plans. As with other accounting standards, as they evolve or change, the Office of the Comptroller will consider the impact of the changes on the Province's accounting.*
We recommend the Office of the Comptroller review and document, on an annual basis, the indexation assumption based on expected level of indexation.	*The Office of the Comptroller feels that the assumptions used in the valuation for accounting purposes were appropriate under current accounting standards. We will continue to evaluate assumptions on an annual basis.*
We recommend the Office of the Comptroller change the mortality assumption to the new Canadian tables issued by the Canadian Institute of Actuaries and that the rationale for the selection of mortality tables be documented.	*As a member of the Actuarial Valuation Committee for the Province of New Brunswick, the Office of the Comptroller will ensure the mortality tables recently adopted by the Canadian Institute of Actuaries are considered for future accounting valuations.*

4.74	**Need to Align Administration Manual Policy AD6402 – Approval of Payments**
As noted in the prior year, the process used by the New Brunswick Internal Services Agency (NBISA) for making payments is not in alignment with administration manual policy AD-6402 – approval of payments. This policy and respective processes used by the shared services environment, as well as other payment system interfaces used by various government departments, are not appropriately aligned.	

Recommendation	**Comments from Management**
We again recommend the OOC and NBISA work together with regard to administration manual policy AD-6402 and align the policy and processes to reflect current payment approval requirements for processing government transactions.	*The Office of the Comptroller will work with the New Brunswick Internal Services Agency to align the policy and processes for the approval of payments.*

4.75	Need to review allowance for doubtful accounts – loans and accounts receivable

During our audit, we noted the following items relating to calculation of allowance for doubtful accounts (AFDA):

1. Loans administered under the *New Brunswick Housing Act*: AFDA for housing loans is calculated by the Department of Social Development using a pre-determined threshold and not based on past collection history. Actual results are not compared after year end to ensure the estimate was accurate.
2. Loans administered under the *Post-Secondary Student Financial Assistance Act*: A current year analysis was not performed by the Department of Post-Secondary Education, Training and Labour to support the AFDA estimate for student loans. An AFDA analysis prepared in fiscal 2012 was carried forward even though more current information suggests an increase in the AFDA estimate is necessary.
3. Loans administered under the *Agriculture Development Act* and the *Fisheries and Aquaculture Development Act*: AFDA estimates provided by the Department of Agriculture, Aquaculture and Fisheries did not contain support for analysis used in calculating the AFDA estimate for each loan outstanding.
4. Department of Justice, court fines receivable: AFDA estimates provided by the Department of Justice did not contain support for the analysis used in calculating the estimate.

During our audit, we also noted no review or formal approval of these AFDA estimates for these Departments. AFDA estimates should be formally documented, reviewed and compared for accuracy subsequent to year end to ensure the estimate process is thorough and robust.

Recommendation	Comments from Management
We recommend the Departments of Social Development, Post-Secondary Education Training and Labour, Agriculture, Aquaculture and Fisheries and Justice provide the Office of the Comptroller with an analysis of the AFDA estimates on an annual basis. This analysis should be formally documented, reviewed and compared to actual results for accuracy subsequent to year end. The Office of the Comptroller should review such analysis provided by the Departments to ensure the estimate is sufficiently supported.	*The Office of the Comptroller will continue to work with all departments to ensure the methodologies used to estimate allowance for doubtful accounts are supported and appropriate.*

4.76	**Need to update estimate of federal tax revenues**

Corporate Income Tax and Personal Income Tax revenue and payments are determined using official estimates and other estimate information exchanged with the Federal Government. Estimate information is provided to the Federal Government to determine tax revenue payments and should be updated for significant new information. If the estimate is inaccurate compared to actual data the Province will owe (or receive) the difference.

During this year's audit we asked to examine the updates to the initial estimate provided to the Federal Government. We were not able to view this information and we were informed the Department of Finance does not update their estimates with the Federal Government based on updated data or recent historical information. Economics and recent history should be considered for application to the estimates to ensure amounts are recorded using management's best estimate based on updated information as it becomes available. The information sent to the Federal Government to update previous estimates should be retained for audit purposes.

Recommendation	Comments from Management
We recommend the Department of Finance update their estimates as necessary using current information and retain such supporting documentation for audit purposes.	*The Federal Government is responsible for establishing and updating estimates for Corporate Income Tax and Personal Income Tax revenue. Official estimates received from the federal government are used as the basis for determining federal tax revenue in the Province's financial statements. Federal tax revenue amounts for the current year reflect prior year adjustments based on returns or more recent economic data. Federal estimates are updated three times a year at set times. At these times, the Province provides updated information to the Federal Government for use in updating its estimates. The information provided to the Federal Government and the confirmation of the information received by the Federal Government is retained on file. The Department of Finance will review the methodology used to determine federal tax revenue and ensure it reflects management's best estimates.*

4.77	**Classification of accounts in the consolidated financial statements**
During our audit we noted some account classifications in the consolidated financial statements for which, at the time our audit, we were not able to obtain satisfactory audit support. We have provided a list of such items to the Office of the Comptroller so that their classification can be reviewed and documented prior to the next year's financial statement audit.	

Recommendation	**Comments from Management**
We recommend the classification of the financial statement elements be analyzed by the Office of the Comptroller to ensure satisfactory support exists for financial statement classifications.	*The Office of the Comptroller will review the financial statement elements outlined and ensure satisfactory support exists for their classification.*

4.78	**Tangible capital assets (TCA) – communication of tangible capital asset policy and asset impairment assessment**

Per Canadian Public Sector Accounting Standard PS2500 – Basic Principles of Consolidation, Government financial statements should consolidate governmental units line-by-line on a uniform basis of accounting after eliminating inter-governmental unit transactions and balances.

In fiscal 2013, the Province of New Brunswick modified the tangible capital asset policy to capitalize information system assets. However during the audit, we noted not all consolidated entities are capitalizing information system assets in a consistent manner. Although this inconsistent application of accounting policy does not currently represent a material misstatement upon consolidation, there is potential a material misstatement could occur in the future as consolidated entities continue to expense purchases that may be capitalized under the Province's current TCA capitalization policy. Based on inquiries with the Office of the Comptroller, their staff were not aware of any communication made to inform the consolidated entities of this accounting policy change. Communicating provincial accounting policy changes to Crown Agencies in a timely manner would assist in consistent application of accounting policies for consolidation purposes.

Additionally, assessments of asset impairment were not documented during the current year. There was no evidence available during our audit of how management reviewed assets for possible impairment or documentation of judgments applied in this process. Such documentation should be prepared and updated each year to help ensure the accounting treatment is in alignment with Canadian Public Sector Accounting Standards.

Recommendations	Comments from Management
We recommend the Office of the Comptroller communicate all provincial accounting policy changes to consolidated entities to ensure accounting policies are applied on a consistent basis upon consolidation. We recommend upon consolidation the Office of the Comptroller quantify the effect of inconsistent application of accounting policies, if the consolidated entities accounting policies are different from the Province. **We recommend the Department of Transportation and Infrastructure prepare and submit to the Office of the Comptroller for review an annual assessment of asset impairment. This documentation should be prepared annually and note areas involving significant judgment or estimates.**	*The Office of the Comptroller will formalize the process for quantifying and documenting the effects of different accounting policies for tangible capital assets. We would like to note that consolidated entities are not obligated to follow Provincial accounting policies. Accounting policies for consolidated entities are set individually by the organization based on their operational needs and materiality. When necessary, adjustments for differences in accounting policies are accounted for during the consolidation process.* *The Office of the Comptroller will work with all departments to establish guidelines and procedures to document the assessment of asset impairment.*

4.79	Grants/government transfers – need for accounting analysis

We were pleased to receive the PS 3410 Government Transfers analysis during the current year as per our prior year recommendation. However, we noted throughout our provincial expenditure testing, not all transactions coded to primary 7 (grants) accounts in Oracle were analyzed in accordance with PS 3410. A number of these transactions appear to be services rather than grants and therefore additional analysis is required to determine if they have been accounted for appropriately in accordance with PS 3410 (e.g. Services related to Local Service Districts).

Recommendation	Comments from Management
We recommend Oracle primary 7 accounts be analyzed to determine whether transaction coding is appropriate. For significant transactions, if the expense coding is appropriate, the transaction should be analyzed to determine if it is in compliance with PS 3410.	*The Office of the Comptroller agrees to review the classification of transactions coded in Primary 7 accounts. We will continue to review the accounting for transactions that fall under the PS 3410 standard to ensure it is appropriate regardless of the account code classification.*

4.80	Write off of accounts and loans receivable policy

It was noted during our audit, write-offs for accounts and loans receivable are not completed in a timely manner. The policy indicates Board of Management is required to approve receivable write-offs before they can occur. This in turn results in a delay in the process and the gross accounts receivable and Allowance for Doubtful Accounts balances are overstated in the Province's consolidated financial statement schedules. In addition schedule 20 of the financial statements lacks transparency as the allowance for each reported receivable is not identified in the schedule.

A further concern is that there is no regular or annual departmental presentation to the Board of Management to review older non-collectable or statute barred receivables. Department presentations to the Board of Management regarding receivables should ideally occur on an annual basis in the fourth quarter of the fiscal year to ensure the Province's financial statements contain the most realistic and accurate receivables value.

Recommendations	Comments from Management
We recommend the Office of the Comptroller amend the write-off policy to require departments to present to the Board of Management at a minimum annually and ideally in the fourth quarter, receivable adjustments and write-offs. **We also recommend the presentation of the accounts receivables balance in the schedules of the financial statements be updated to identify allowance for doubtful accounts amounts for each reported receivable grouping.**	*The Office of the Comptroller will consider, as part of its future planning, a review of Administration Manual policy AD-6307 Deletion of Debts. A review of alternate presentations of the accounts receivable and allowances for doubtful accounts included in schedule 20 of the financial statements will also be considered.*

4.81	**Property Tax Revenue - Municipal Suspense Account Reconciliation**

During the year, the Department of Finance identified an error in the municipal revenue suspense account (account 1121) resulting from prior year. The error was caused last year when the Department was reconciling the 1121 account and encountered a large unexpected variance in the account. To reduce the variance, the Department posted an entry in error. The amount of the entry was $4.3 million. This situation indicates challenges still exist in reconciling the 1121 municipal suspense account.

This year the Department was able to provide an explanation for the variance in the 1121 account, however, some difficulties arose when providing documentation to support the explanation. The Department should review the various entries posted to the 1121 account (municipal revenue suspense) as these entries have a direct impact on the amount of provincial revenue recorded. The Department should also maintain documented evidence to support any variances in this account.

Recommendations	Comments from Management
We recommend the Department perform a detailed analysis of the entries posted to the municipal revenue suspense account to ensure they are correct. **We recommend the Department maintain documented evidence to support the variance in the municipal revenue suspense account.**	*The Department of Finance agrees with the recommendation and will implement a monthly reconciliation process for the municipal revenue suspense account.*

4.82	Netting of Property Tax Revenue

During the audit, we noted a number of instances where provincial tax revenue was reduced inappropriately. For example, we noted revenue was reduced by $7.3 million for the clearing of the 1121 municipal revenue suspense account. We also noted revenue was reduced by $2 million for appeals relating to municipal taxes. PSAB standards require financial statements disclose the gross amount of revenues. Reducing or netting revenue for the above items is not appropriate accounting treatment and these items should be more appropriately recorded as expenses.

Recommendations	Comments from Management
We recommend the Department of Finance record the gross amount of property tax revenue in the financial statements. **We recommend the Department of Finance record the clearing of the municipal suspense account and the portion of tax appeals relating to municipal taxes as expenses in the financial statements.**	*The Department of Finance agrees with the recommendation and will report these adjustments as expenditure. The process to create the expense account is underway with the Budget and Financial Affairs Division.*

4.83	Support for and Review of Changes to Property Tax Assessment Values

In our sample of 29 properties, we noted one instance where the assessed value of a property was changed as the result of a request for review. The property card we were provided did not contain any documentation or support for the re-assessed property value. We inquired with SNB assessment staff and were informed they were unable to provide any documentation or support for the re-assessed value. Without proper support for the assessment, there is risk the property is not assessed at its real and true value.

Recommendation	Comments from Management
We recommend all changes made to assessed property values be documented and recorded with the property card. Changes in assessed value should contain a documented sign off and review by the assessor's manager.	*Service New Brunswick has recently deployed electronic data collection equipment. The changes made to property's assessed value will be tracked and the responsible assessor will be required to document the change. Quality Control enhancements will be in place to prevent un-documented changes in assessed value.*

Chapter 5
Matters Arising from our Audits of Crown Agencies and Federal Claims

Contents

Matters Arising from our Audits of Crown Agencies and Federal Claims

Introduction

5.1 In this chapter we discuss our significant findings and recommendations relating to our audits of Crown agencies' financial statements and federal claims.

5.2 We audit the following Crown corporations, Boards, Commissions and other agencies:

- Centre communautaire Sainte-Anne (CCSA)
- Collège communautaire du Nouveau-Brunswick (CCNB)
- Energy Efficiency and Conservation Agency of New Brunswick (EECANB)
- Financial and Consumer Services Commission (formerly New Brunswick Securities Commission) (FCNB)
- Invest New Brunswick (INB)
- Kings Landing Corporation (KLC)
- New Brunswick Agricultural Insurance Commission (NBAIC)
- New Brunswick Community College (NBCC)
- New Brunswick Electric Finance Corporation (NBEFC)
- New Brunswick Highway Corporation (NBHC)
- New Brunswick Immigrant Investor Fund (2009) Ltd. (NBIIF)
- New Brunswick Internal Services Agency (NBISA)
- New Brunswick Legal Aid Services Commission (LA)
- New Brunswick Lotteries and Gaming Corporation (NBLGC)
- New Brunswick Municipal Finance

Corporation (NBMFC)
- New Brunswick Research and Productivity Council (RPC)
- Premier's Council on the Status of Disabled Persons (PCSDP)
- Provincial Holdings Ltd. (PHL)
- Public Trustee - Trusts administered (PT)
- Regional Development Corporation (RDC)

5.3 We also audit the following Federal claims:

- Agreement on Labour Market Development
- Agreement on Targeted Initiative for Older Workers
- Agreement on the Transfer of Federal Gas Tax Revenues
- Agreement Respecting Legal Aid and Court-Ordered Counsel
- Agreement for Saint John Harbour Bridge Rehabilitation
- Agreement on the Transfer of Federal Public Transit Funds
- Building Canada Fund– Communities Agreement
- Building Canada Infrastructure Plan – Base Funding Agreement
- Strategic Infrastructure Agreement for Improvements to the National Highway System

5.4 To reach an opinion on the Crown agencies' financial statements and federal claims, we carry out audit work on the major programs and activities in Crown agencies or departments. In addition, we audit major transactions and account balances, and examine internal controls of significant computerized systems.

5.5 In almost every audit, matters arise that need to be discussed with management. Except in cases where an audit opinion is qualified, these matters, although significant, are not sufficiently large in dollar or qualitative terms to affect our opinion on the financial statements. It is our practice to report these matters to senior officials of the agencies/departments concerned, and to ask for a response. Some of these findings may not be included in this Report, because we do not consider them to be of sufficient importance to bring to the attention of the Legislative Assembly, or because public attention to internal control weaknesses, before they are corrected, could possibly result in loss of government assets. For further background on our audit objectives refer to Appendix I.

5.6 We are reporting significant audit findings from the fiscal years ended 2014 and 2013, 2012 or 2010 depending on the timing of the completion of our audit work relative to the printing of the Auditor General's Annual Report.

5.7 We had several findings from our audits of Crown agencies' financial statements and federal claims. We review the findings identified to determine which findings from our work are significant. When considering which findings are significant we assess:

- dollar magnitude of the item;
- the risk the finding could result in a large loss or error in future;
- the number of instances the finding has occurred;
- if the finding has occurred in multiple entities;
- if the finding was reported in a prior year; and
- if we believe the finding is overall significant in nature.

Highlights and Recurring Themes

5.8 Highlights and recurring themes of our significant findings are presented in Exhibit 5.1.

Exhibit 5.1 - Highlights and Recurring Themes

	Entity where concern was noted for 2014 AG Report	Concern in this area also noted in 2013 AG Report	Concern in this area also noted in 2012 AG Report
Accounting Concerns	CCNB	Yes	
	EECANB	Yes	
	FCNB		
	INB		
	KLC		Yes
	LA		
	NBAIC		

Shaded Crown entities indicate a concern in this area was also noted in the 2013 or 2012 AG Reports
Continued on following page

Exhibit 5.1 - Highlights and Recurring Themes (continued)

	Entity where concern was noted for 2014 AG Report	**Concern in this area also noted in 2013 AG Report**	**Concern in this area also noted in 2012 AG Report**
Accounting Concerns (continued)	NBCC	Yes	Yes
	NBHC		
	NBIIF		
	NBISA		
	PHL		
	RDC		Yes
Lack of Segregation of Duties	CCNB	Yes	
	EECANB	Yes	
	INB	Yes	Yes
	KLC		Yes
	LA	Yes	Yes
	NBAIC	Yes	
	NBCC	Yes	Yes
	NBIIF		Yes
	NBISA		Yes
	PHL		
	RDC		
Oversight/Governance Concerns	CCNB		
	EECANB		
	INB	Yes	
	LA		
	NBAIC	Yes	Yes
	NBIIF		
	NBISA	Yes	
	PHL		
	RDC		Yes
Accounting/Documentation Concerns With Estimates	CCNB	Yes	
	EECANB	Yes	Yes
	NBAIC		
	NBCC	Yes	Yes
	NBHC		Yes
	PHL		
	RDC		Yes
Management of Agreements or Third Party Arrangements	CCNB		
	NBCC		

Shaded Crown entities indicate a concern in this area was also noted in the 2013 or 2012 AG Reports

5.9 We are concerned that a number of these findings were observed across different agencies/departments. As a result of the same issue arising in different entities we saw recurring themes emerge over the course of our work. Exhibit 5.1 shows the agencies/departments where we noted these recurring themes. Due to the significance of the issues and/or the number of instances observed, we have chosen to highlight these recurring themes in this chapter.

Accounting concerns

5.10 There were several accounting concerns noted in our Crown agency audits involving 13 Crown agencies. Five of these 13 Crown agencies also had a finding regarding accounting concerns in either of our 2013 or 2012 Reports. Accounting concerns should be resolved in advance of our audit to ensure the Board or oversight entity of the Crown agency is receiving accurate and complete financial information during the year.

5.11 Areas involving accounting concerns most often occurred regarding management not being aware of changes to accounting standards or not applying new accounting standards properly. In all cases, the accounting concerns related to a concern observed during our audit, that required our office's time to address or resolve prior to issuing our audit opinion.

5.12 It is our view that Crown agencies should have sufficient knowledgeable resources available to ensure the accounting standards are appropriately followed. The occurrence of the annual financial statement audit does not fulfil the board or management's responsibility to ensure adequate financial accounting expertise has been applied in the Crown agency's financial reporting.

Lack of segregation of duties

5.13 We observed 11 Crown agencies where we had concerns regarding proper segregation of duties. Of these 11 Crown agencies, nine also had a segregation of duties finding in our 2013 or 2012 Reports. Proper segregation of duties ensures the preparer and reviewer functions are performed by different people to eliminate the possibility of accounting work not being reviewed or being reviewed by the person who prepared it. Sometimes this also involves ensuring a proper segregation of duties in the accounting software or ensuring appropriate policies are in place to direct that preparer and approval roles are required to be separated.

5.14 Normally a lack of segregation of duties is an indication of an accounting system weakness such that fraud or error could occur. When we note a lack of segregation of duties our auditors normally perform extra procedures to mitigate against the risk of fraud or error in the financial statements. We encourage Crown agencies to review their financial processes to ensure financial processes are appropriately structured and that appropriate approval processes are present.

5.15 We also encourage Crown agencies to be alert to potential segregation of duties concerns during agency restructurings or staff reorganizations. Safeguards should be in place so that separation of key accounting duties is maintained before and after any reorganization/restructuring activity.

Oversight/governance concerns

5.16 There were nine Crown agencies noted in our audits where we had concerns regarding oversight or governance processes. These concerns varied by entity and included items such as: weaknesses in conflict of interest disclosures, lack of an audit committee, lack of regular board meetings, lack of risk management or internal control oversight and other oversight/governance weaknesses.

5.17 We noted four of these Crown Agencies also had oversight/governance concerns reported in either of our 2013 or 2012 Reports. Effective oversight or "tone at the top" is important to building a strong internal control and risk management foundation for any Crown agency. We encourage those Crown agencies to address these concerns.

Accounting/documentation concerns with estimates

5.18 We had concerns with the accounting and documentation process for estimates in seven Crown agency financial statement audits. Of these seven, five had an issue noted in either of our 2013 or 2012 Reports regarding estimates.

5.19 In six of the seven Crown agencies where we noted concerns this year, the primary aspect of concern related to estimates supporting receivables balances (either accounts receivable or loans receivable), however concerns regarding estimates were also noted for deferred revenues, tangible capital asset values and environmental liabilities.

5.20 Estimates involve the application of judgment to quantify unknown or uncertain amounts. Current auditing standards require that we examine estimates with more rigor, including reviewing the estimate's accuracy by comparing the estimate to current known outcomes and past accuracy history. This is an important process to ensure estimates are appropriate and supported.

5.21 In our audits we also noted a lack of appropriate support for management estimates. Management should document and support significant estimates used in preparing the financial statements. Support for significant estimates should also be reviewed by a second person other than the preparer.

Management of agreements or third party arrangements

5.22 We noted in both provincial community colleges concerns regarding agreements with the Province. Key aspects of the operating arrangements such as accounting for improvements to buildings and accounting for certain employee benefits have not been clearly documented.

5.23 While we have observed satisfactory information to form our audit opinion, the colleges and the Province need to document these arrangements to ensure a common, clear understanding and to provide enhanced support for the current accounting treatment.

5.24 Further, this concern may also be present for any other Crown agencies we do not audit. We encourage all Crown agencies to ensure there is a clearly documented understanding of the responsibilities/rights/obligations of the Crown agency and the Province to support significant accounting decisions contained in the Crown agency financial statements.

Applicability to other Crown agencies

5.25 We note a number of these themes from Crown agency comments have occurred in our prior years Reports. We encourage management of all Crown agencies to review these highlights and themes to consider if further improvements or adjustments are needed in their own organization.

Timeliness of Crown agency audits and financial reporting

5.26 We have also noted a recent trend in late completion of Crown agency audits. We acknowledge some of this situation is due to our office's own lack of staff resources to complete Crown agency audits in a more timely manner (especially in 2014 given the early completion of the Province of New Brunswick financial statement audit).

5.27 However, we note that some Crown agencies are more than one financial reporting cycle behind at time of finalizing this chapter including: New Brunswick Lotteries and Gaming Corporation, Energy Efficiency and Conservation Agency of New Brunswick, New Brunswick Immigrant Investor Fund (2009) Ltd. and Public Trustee - Trusts administered.

5.28 For these Crown agencies, the March 31, 2013 audited financial statements were not yet released at the time of finalizing this chapter. We see this as an undesirable trend with risk of growth.

5.29 Producing audited financial statements 18 months or more after the fiscal year end is still necessary, but the exercise holds much less value to the public and other users of this information if the reporting is not performed in a more timely manner. We strongly encourage all Crown agencies to promptly complete their financial reporting obligations.

Conclusion

5.30 While we have not noted any significant fraud, theft or error, the existence of the findings noted in Exhibit 5.1, increases the risk of loss or mistake in the agency's/department's financial reporting. These items should be addressed prior to the next audit cycle.

Appendix I - Audit Objectives

5.31 Our examination of the matters included in this chapter of our Report was performed in accordance with Canadian generally accepted auditing standards, including such tests and other procedures as we considered necessary in the circumstances. The matters reported should not be used as a basis for drawing conclusions as to compliance or non-compliance with respect to matters not reported.

5.32 We obtain reasonable assurance on the financial statement figures because it would not be cost effective to obtain absolute assurance - our auditors cannot test every transaction.

5.33 By applying audit procedures to test the accuracy or reasonableness of the figures appearing in the financial statements, we achieve our desired level of assurance. We use audit procedures such as tracing samples of transactions to supporting documents, examining the effectiveness of certain internal controls, confirming year-end balances with third parties and reviewing the reasonableness of estimates.

5.34 Because of the limited objectives of this type of audit work, it may not identify matters which might come to light during a more extensive or special examination. However, it often reveals deficiencies or lines of enquiry which we might choose to pursue in future audit work.

Responsibilities of Crown Agencies and Government

5.35 The Crown agencies or departments are responsible for the preparation and the content of the financial statements or claims in accordance with the applicable accounting framework. When preparing the financial statements or claims, significant estimates may be made by the auditee, as not all information is available or determinable at the time of finalizing the statements.

Responsibilities of the Office of the Auditor General

5.36 Our Office is responsible for auditing the financial statements or claims listed in paragraphs 5.2 and 5.3. An audit provides reasonable, but not absolute, assurance that the financial statement(s) or claim(s) are free of material misstatement or are in compliance with the relevant agreement. Material misstatement refers to an item or group of items that, if omitted or misstated, would alter the decisions of reasonably knowledgeable financial statement users. The tolerable level of error or misstatement is a matter of judgment.