

## Chapter 1

### Section 1.15

# Toward Better Accountability—Quality of Annual Reporting

Follow-Up on VFM Chapter 4, *2017 Annual Report*

#### RECOMMENDATION STATUS OVERVIEW

	# of Actions Recommended	Status of Actions Recommended				
		Fully Implemented	In the Process of Being Implemented	Little or No Progress	Will Not Be Implemented	No Longer Applicable
Recommendation 1	3	3				
Recommendation 2	2	2				
Recommendation 3	1	1				
Recommendation 4	2	2				
Recommendation 5	2	2				
<b>Total</b>	<b>10</b>	<b>10</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>%</b>	<b>100</b>	<b>100</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>

### Overall Conclusion

As of March 29, 2019, the Treasury Board Secretariat had fully implemented 100% of actions we recommended in our *2017 Annual Report*. For example, the Agencies and Appointments Directive was amended, effective January 1, 2019, to require that board-governed provincial agencies include outcome-based reporting in their annual reports.

Although the Secretariat did not implement some of the actions in the manner we recommended, appropriate alternative actions taken

have addressed the issue. These recommendations primarily refer to amending the Broader Public Sector Business Documents Directive to ensure that it requires organizations to improve their annual reporting. The Secretariat has amended guidance material and communicated our recommendations to organizations. Best practices include information on costs of results achieved and, for broader-public-sector organizations, to base performance measures and targets on outcomes to be achieved. These actions inform the organizations of best practices and are a positive step toward better accountability.

The status of actions taken on each of our recommendations is described in this report.

## Background

A public-sector organization’s annual report, including its audited financial statements, provides details about the organization’s activities, and is meant to give the responsible minister, all members of the Legislature and the public a comprehensive view of the organization’s operational and financial performance. The annual reporting requirements of provincial agencies and broader-public-sector (BPS) organizations are typically governed by the statute that created the agency, a Memorandum of Understanding (MOU) between the agency and its responsible minister, and/or a directive of Management Board of Cabinet.

Government directives stipulate the mandatory content of most agencies’ annual reports. In addition, the Public Sector Accounting Board (PSAB) has issued a Statement of Recommended Practice (SORP) with respect to the reporting of supplementary information beyond that presented in the financial statements. SORP provides general guidance to organizations, including those that prepare an annual report. These reporting practices are encouraged but not mandatory.

In 2017, we reviewed how agencies’ annual reports adhere to government directives and to SORP’s guidelines regarding annual reports. Specifically, we examined one directive that applied to provincial agencies and another that applied to broader-public-sector organizations, and compared their mandatory requirements to the information encouraged by SORP.

These are the main observations and findings in our *2017 Annual Report*:

- Provincial agencies and broader-public-sector organizations are required by directive to include performance targets in their annual reports. SORP encourages performance measures and their related targets to be “outcome”-based rather than just “output”-based.
- Provincial agencies and broader-public-sector organizations are required by directive to include an analysis of their performance in their annual reports or other information they make available to the public (provincial agencies must analyze both their financial and operational performance; broader-public-sector organizations are required to analyze just their operational performance). SORP encourages that analysis to include the significant risks and other factors that affected performance, and explain what that effect was.
- SORP encourages annual reports to inform readers of the costs of the performance results achieved, thus linking financial and non-financial performance information.
- Based on our review of the annual reports of 27 provincial agencies and broader-public-sector organizations, we noted that two 2015/2016 annual reports met all the selected SORP criteria (AgriCorp and Algonquin Forestry Authority). Four other annual reports in our sample met all but one criterion: the Liquor Control Board of Ontario (LCBO), the Ontario Energy Board, Ontario Power Generation and the Ontario Lottery and Gaming Corporation. These six entities included in their annual reports performance measures that were clear and included performance targets. Their annual reports also included thorough financial and variance analysis (except AgriCorp, as no significant variances were identified).
- With respect to compliance with the Agencies and Accountability Directive, we noted that nine (60%) of the 15 provincial agencies’ 2015/16 annual reports we reviewed met all the selected Directive criteria, with an additional two (13%) annual reports meeting all but one criterion. All annual reports included audited financial statements as required by the Directive. Seven (50%) of the 14 broader-public-sector organizations’ websites

we reviewed met the Broader Public Sector Business Documents Directive's requirement to include certain key information all on one web page. Another two broader-public-sector organizations had all the information required by the selected Directive criteria on their websites, although not always on one web page, for a total of nine organizations (64%) having all the required information on their websites.

We made five recommendations, consisting of 10 action items, to address our findings and received commitment from the Treasury Board Secretariat that it would take action to address our recommendations.

## Status of Actions Taken on Recommendations

We conducted assurance follow-up work between May 2019 and July 2019. We obtained written representation from the Treasury Board Secretariat that effective November 1, 2019, it had provided us with a complete update of the status of the recommendations we made in the original review two years ago.

### Statement of Recommended Practice (SORP) Encourages Annual Reports to Include Information beyond Directive Requirements

#### Recommendation 1

*To improve the quality of the annual reports of provincial agencies and broader-public-sector organizations, we recommend that Treasury Board Secretariat propose to Treasury Board/Management Board of Cabinet that the Agencies and Appointments Directive and the Broader Public Sector Business Documents Directive be amended to include the following requirements for annual reports:*

- *base performance measures and targets on outcomes to be achieved (that is, in terms of improved consequences) rather than solely on outputs;*

**Status: Fully implemented.**

#### Details

The Public Sector Accounting Board's (PSAB's) Statement of Recommended Practice (SORP) encourages public-sector entities to provide useful information that goes beyond the information their directives require them to include in their annual reports. For example, the Agencies and Appointments Directive required that an annual report include a discussion of performance targets achieved and analysis of operational performance. However, the SORP specifically suggests that performance measures should be stated in terms of outputs and also outcomes. Of the 11 of 15 provincial agency annual reports that contained clear performance measures, six (55%) contained strictly output-based measures, while five (45%) included outcome-based measures. Of the seven of 12 broader-public-sector (BPS) organization annual reports that contained clear performance measures, one (14%) contained strictly output-based measures, while six (86%) included outcome-based measures.

Since then, Treasury Board Secretariat has amended the Agencies and Appointments Directive, effective January 1, 2019, to require that board-governed provincial agencies include outcome-based reporting in their annual reports. As well, it has provided additional guidance on developing outcome-based measures to provincial agencies.

The requirement to include outcome-based reporting in a provincial agency's annual report is being implemented as a phased approach over three years to allow board-governed agencies to increase the capacity and quality of their reporting over time.

For BPS organizations, Treasury Board Secretariat has addressed this recommendation sufficiently by updating online supporting

guidance identifying best practices, including basing performance measures and targets on outcomes to be achieved.

- *identify significant risks and other factors that have impacted performance and results, explain the impacts, and report on plans to mitigate the risks;*

**Status: Fully implemented.**

#### Details

Without a thorough discussion of risks in an agency's annual report, the Legislature and the public cannot assess what challenges the entity is facing, the impact of those risks on performance and possible mitigating strategies.

In 2017, we found that the Agencies and Appointments Directive required that risks and related risk-management plans be included in business plans for provincial agencies. However, it did not require any risk information for annual reports. It also did not require that the business plans discuss how those risks affect performance. For the five of the 15 provincial agencies (33%) that included information in their annual reports on the risks the agency was facing, we noted that the risks were clearly identified and there were explanations of how these risks were managed.

The BPS Business Documents Directive did not require that the annual report disclose risks affecting the organization, the impact on performance (if any) and related mitigating strategies. As a result, only one of the 12 (8%) BPS organizations' annual reports in our sample contained a risk analysis.

Since then, Treasury Board Secretariat has amended the Agencies and Appointments Directive, effective January 1, 2019, to require that board-governed provincial agencies include in their annual reports a description of how risk events and other significant factors impact the results achieved. Updated guidance material also states an expectation that the annual report should include an analysis of risk events and, to provide a complete picture of the risk, a discussion of the mitigation strategy.

Treasury Board Secretariat has addressed this recommendation sufficiently by updating online supporting guidance identifying best practices, which include identifying significant risks and other factors that have impacted performance and results, explaining the impacts, and reporting on plans to mitigate the risks.

- *report on the costs of results achieved.*

**Status: Fully implemented.**

#### Details

SORP encourages annual reports to contain information to inform readers of the costs of the performance results achieved, thus linking financial and non-financial performance information. Four of the 15 provincial agency annual reports and none of the 12 BPS organization annual reports contained this information linking costs to results. Ontario Power Generation's annual report contains this type of information. The linking of financial and non-financial performance information helps the reader assess how the entity used its resources during the reporting period and what was achieved as a result of the resources expended.

Treasury Board Secretariat has addressed this recommendation sufficiently by updating its guidance material to both provincial agencies and BPS organizations to encourage reporting on the costs of results achieved. This has not been included in the applicable Directive as a requirement because Treasury Board Secretariat is of the view that agencies will not be required to report information that provincial ministries are not required to report. Ministries do not currently report on costs of results achieved.

#### Recommendation 2

*To improve the quality of the annual reports of broader-public-sector organizations, we recommend that Treasury Board Secretariat propose to Treasury Board/Management Board of Cabinet that the Broader Public Sector Business Documents Directive be amended to require that these organizations:*

- *analyze their financial performance in their annual reports, including discussing variances between their actual financial results against estimates;*

**Status: Fully implemented.**

#### Details

We noted in 2017 that the BPS Business Documents Directive does not require BPS organizations to analyze the organizations' financial performance in the information available to the public (including discussing variances in their actual financial results against estimates). Even though not required by the directive, five of the 13 BPS and other organizations' annual reports we reviewed (38%) did nevertheless contain a financial analysis. This includes Ontario Power Generation, which is not bound by any directive requirements for its annual report. As would be expected when organizations are not required to do so, significant variances were not explained in six (60%) of the 10 annual reports we reviewed that had significant variances.

Treasury Board Secretariat has addressed our recommendation sufficiently by incorporating best practices, including discussing variances in their actual financial results against estimates, in a guideline. Incorporating the recommendations into guidance available publicly online is an alternative approach to strengthen guidance for BPS organizations on annual reporting.

- *include all other performance information in the annual report rather than allowing the information to be either in an annual report or on a webpage showing the organization's business plan.*

**Status: Fully implemented.**

#### Details

Information required by the BPS Business Documents Directive does not have to be in an organization's annual report—it just has to be publicly available and on the same web page on the organization's website. That means the information could be divided up in more than one place—some

of it might be on a web page showing the organization's business plan and some might be in an annual report. SORP specifies that the full range of information it encourages to be reported should be contained in an annual report (which it calls a "public performance report"). Having a "one-stop shop" in the form of an annual report with all of an organization's financial and operational performance information would be more helpful and useful for stakeholders.

Treasury Board Secretariat has addressed our recommendation sufficiently by amending its guidance to BPS organizations to state that including performance information in the annual report rather than in separate business documents is a best practice. This guidance also includes a link to our 2017 report to encourage organizations to review our recommendations in order to be aware of best practices.

#### Recommendation 3

*To ensure that the annual reports of public-sector entities that fall outside the scope of existing directives contain useful and thorough information, we recommend that Treasury Board Secretariat propose to Treasury Board/Management Board of Cabinet that authoritative direction be provided regarding the information they must contain.*

**Status: Fully implemented.**

#### Details

In 2017, we noted that some public-sector entities fall outside the scope of both the Agencies and Appointments Directive and the BPS Business Documents Directive. In the absence of a directive mandating what their annual reports must contain, these entities have the option of following the guidance available for public-sector organizations, but they are not required to do so.

Since then, Treasury Board Secretariat requested the Ministry of Energy, Northern Development and Mines to ensure that Ontario Power Generation (OPG) and the Independent Electricity System Operator (IESO)—the two

entities outside the scope of the directives, which report to the ministry—are aware of the Auditor General’s recommendations regarding the content of annual reports. In connection with this, Treasury Board Secretariat has requested the ministry to share with OPG and IESO information such as updated supporting material relating to the BPS Business Documents Directives and SORP guidelines.

## Annual Reports Do Not Always Identify How the Entity’s Performance Was Measured and the Performance Targets to Be Achieved

### Recommendation 4

*To enable Members of Provincial Parliament and the public to easily assess whether the entity met, exceeded or fell short of its stated targets, we recommend that the Treasury Board Secretariat, in conjunction with ministries, take action to help ensure that:*

- *entities clearly identify and disclose performance measures, and, as required by the directive, applicable performance targets and results in their annual reports;*

**Status: Fully implemented.**

### Details

Performance measurement is the process of collecting and analyzing information that indicates how well an entity is performing. Performance should be measured against pre-established goals, or targets. In 2017, we noted that four of the 15 provincial agency annual reports we reviewed (27%) did not clearly identify the performance measures of the agency, and four did not disclose or identify the performance target. For broader-public-sector (BPS) organizations we noted that five of the 12 BPS organization annual reports we reviewed (43%) did not clearly identify the performance measures of the organization, and seven did not disclose or identify the performance target.

Treasury Board Secretariat amended the Agencies and Appointments Directive, effective January 1, 2019, to require that board-governed provincial agencies explicitly add performance measures to existing requirements for targets, and has updated the guidance for this requirement. As well, Treasury Board Secretariat has updated guidance to the BPS Business Documents Directive to reflect this best practice.

Treasury Board Secretariat also provided ministries with a template letter to communicate with provincial agencies the changes in expectations for annual reports. In March 2019, Treasury Board Secretariat informed all ministries that the supporting material for the BPS Business Documents Directive had been updated and asked ministries to encourage organizations to review the Auditor General’s recommendations on annual reporting. It also reminded ministries to consult this supporting documentation when reviewing the annual reports of designated BPS organizations, and that ministerial approval of the provincial agencies’ annual reports “indicates agreement that the report meets the form and content requirements set out in the directive and/or other relevant direction.”

- *when targets are not met, as required by the directive, the annual report include planned actions to achieve these targets in the future.*

**Status: Fully implemented.**

### Details

Of the 15 annual reports we sampled that reported performance targets (54% of the 28 reviewed), three (20%) did not include a discussion of the reported result or outcomes. This discussion is crucial for the entity to identify where it did not meet the target and the reasons why. It is also an opportunity for the entity to discuss possible strategies to address the shortfall.

As noted above, Treasury Board Secretariat has taken action, in conjunction with the ministries, to notify provincial agencies and designated BPS organizations of the 2017 recommendations, including the requirement for the annual report to

include planned future actions to address achieving targets that were not met.

## Financial and Variance Analysis Could Be Improved

### Recommendation 5

To provide readers of provincial agency annual reports with a thorough understanding of agencies' financial performance, we recommend that Treasury Board Secretariat propose to Treasury Board/ Management Board of Cabinet that:

- the Agencies and Appointments Directive be amended to include a definition of what a significant variance is;

**Status: Fully implemented.**

#### Details

Although reasons for variances in financial performance are to be included in provincial agencies' annual reports, the Agencies and Appointments Directive does not define a variance that is significant enough for inclusion. As a result, agencies must determine what they believe is reasonable to include as significant variances. Of the 15 provincial agency annual reports we sampled, four (31%) did not have any discussion of significant variances.

Since then, Treasury Board Secretariat has amended the Guide to Developing Annual Reports to include criteria for determining when a variance is significant. The criteria incorporates the SORP factors for determining what is crucial to an organization, including criteria such as financial magnitude and importance to the overall success of the entity.

While the Agencies and Appointments Directive was not updated to include a definition of what a significant variance is, updating the Guide addresses our recommendation sufficiently by providing guidance as to what constitutes a significant variance.

- in conjunction with ministries, it take action to help ensure that financial performance analysis, including explanations for significant variances, be included in all provincial agency annual reports.

**Status: Fully implemented.**

#### Details

In 2017, we noted that five (33%) of the 15 provincial agency annual reports we examined did not contain an analysis of financial performance. As noted above, four (31%) of the 15 provincial agency annual reports we sampled did not have any discussion of significant variances.

The Agencies and Appointments Directive was updated in January 2019 to clarify the ministry's role in the approval of the annual report of an agency that reports to it. The Directive now states that "ministerial approval indicates agreement that the annual report meets the form and content requirements as specified in the directive and any agency-specific content as required by the relevant minister or applicable legislation."

As mentioned, Treasury Board Secretariat has also updated guidance for agencies to incorporate suggested information into their annual reports. The Secretariat has also communicated with ministries, and provided a template letter for them to use to communicate with provincial agencies, the changes in expectations for annual reports. This template letter also refers to the clarification in the directive that "ministerial approval of annual reports indicates agreement that the report meets the form and content requirements set out in the directive and/or other relevant direction."

## Overall Comment

Treasury Board Secretariat has taken a number of positive steps forward in addressing our recommendations, including amending the Agencies and Appointments Directive and applicable guidance for BPS organizations. These steps will help to promote compliance with best practices in annual reporting.

We continue to encourage the Secretariat to pursue applicable changes to the BPS Business Documents Directive to ensure that best practices are a requirement, rather than being referred to only in guidance material.

### Recommendation

*To improve the quality of the annual reports of broader-public-sector organizations, we recommend that Treasury Board Secretariat propose to Treasury Board/Management Board of Cabinet that the Broader Public Sector Business Documents Directive be amended to include requirements that the best practices that are currently included in guidance material be followed, including:*

- *requiring that base performance measures and targets be aimed at outcomes to be achieved (which specify improved consequences) rather than only at outputs to be reached;*
- *requiring that organizations identify significant risks and other factors that have impacted their performance and results, explain the impacts and report on plans to mitigate the risks; and*
- *requiring that organizations analyze their financial performance in their annual reports, including discussing variances between their actual financial results and their estimates.*

## Treasury Board Secretariat Response

The Treasury Board Secretariat (Secretariat) is committed to enhancing transparency and accountability with respect to the content of annual reports. The Secretariat is also committed to providing information to members of the public, supporting ease of access to information about how public money is managed.

The Secretariat will build on the progress made in enhancing supporting material for the broader public sector by reviewing and updating the Broader Public Sector Business Documents Directive to further strengthen direction on the content of performance reports. Consideration will be given to incorporating content identified in supporting material as best practices. The Secretariat will continue to engage partners and stakeholders to ensure that we employ an evidence-based approach to achieving change.

## Chapter 1

### Section 1.16

# Public Accounts of the Province

Follow-Up on Chapter 2, *2017 Annual Report*

#### RECOMMENDATION STATUS OVERVIEW

	# of Actions Recommended	Status of Actions Recommended				
		Fully Implemented	In the Process of Being Implemented	Little or No Progress	Will Not Be Implemented	No Longer Applicable
Recommendation 1	1	1				
Recommendation 2	1	1				
Recommendation 3	2	2				
Recommendation 4	2	1	1			
Recommendation 5	3	3				
Recommendation 6	1			1		
Recommendation 7	1					1
Recommendation 8	1		1			
Recommendation 9	1	1				
Recommendation 10	1	1				
<b>Total</b>	<b>14</b>	<b>10</b>	<b>2</b>	<b>1</b>	<b>0</b>	<b>1</b>
<b>%</b>	<b>100</b>	<b>72</b>	<b>14</b>	<b>7</b>	<b>0</b>	<b>7</b>

### Overall Conclusion

As of October 31, 2019, 72% of the actions we recommended in our *2017 Annual Report* have been fully implemented. For example, since our 2017 audit, the province corrected the accounting in the province's consolidated financial statements to follow Canadian Public Sector Accounting Standards (PSAS). This included recording a valuation allowance for net pension assets, appropriately

recording the impact of the electricity rate reduction and appropriately removing the IESO market accounts from the province's consolidated financial statements.

The province has made progress in implementing a further 14% of the recommended actions. For example, the province is in the process of having the ministries and agencies that consolidate into the province's financial statements request their external advisors to notify our Office of their engagement as required under the Code of Professional Conduct of the Chartered Professional Accountants

of Ontario. The Office of the Provincial Controller Division has been working with stakeholders to identify key areas that impact an earlier delivery of the province's consolidated financial statements.

The province has made little to no progress on one recommendation (7% of the recommended actions) as it has not yet put into legislation any requirements to follow Canadian PSAS.

Additionally, one recommendation (7% of the recommended actions) is no longer applicable due to a change in reporting of government debt.

The status of actions taken on each of our recommendations is described in the following sections.

## Background

For the year ended March 31, 2017, we issued a qualified audit opinion on the consolidated financial statements for the province of Ontario for the following reasons:

- The province did not record a valuation allowance against the net pension asset relating to the Ontario Teachers' Pension Plan and the Ontario Public Service Employees' Union Pension Plan in its consolidated statement of financial position.
- The province inappropriately recorded the market account assets and liabilities of the Independent Electricity System Operator in its consolidated financial statements.

We also included an Other Matter paragraph in the auditor's report because the province inappropriately recognized rate-regulated assets, which is not permitted when applying Canadian Public Sector Accounting Standards (PSAS) to government financial statements. Although this amount was not material to the 2016/17 consolidated financial statements, we were concerned that future statements could become materially misstated if the accounting was not corrected.

The Auditor General was required to issue the qualifications under Canadian Auditing Standards

as the above practices were contrary to Canadian PSAS. Canadian PSAS are the most appropriate accounting standards for the province to use in preparing its consolidated financial statements because they ensure that information about the province's surplus and the deficit is fair, consistent and comparable to data from previous years and from peer governments. This allows all legislators and the public to better assess government management of the public purse.

Annually, we have raised the issue of the prior government having introduced legislation on several occasions to facilitate its establishment of specific accounting practices that may not be consistent with Canadian PSAS. Until now, such actions did not impact the province's consolidated financial statements. The use of legislated accounting treatments by the province to support the accounting/financing design prescribed under the *Ontario Fair Hydro Plan Act, 2017*, could have had a material impact on the annual results and become a significant concern to our Office in the 2017/2018 fiscal year had the accounting not been corrected. More discussion of this issue can be found in our Special Report titled *The Fair Hydro Plan: Concerns About Fiscal Transparency, Accountability and Value for Money*, tabled in the Legislative Assembly on October 17, 2017.

## Additional Issues

### The Government's Use of Consultants

We noted the prior government engaged external advisors to help design the complex accounting/financing structure of the Fair Hydro Plan rate reduction and sought advice from accounting firms on parts of the transaction. However, despite the recommendation made in our *2016 Annual Report* that the government share with our Office any advice or work of external advisors in formulating an accounting position, the government did not inform us of their advisors' work until we became aware that significant discussions were being held

on matters related to the Fair Hydro Plan, and we specifically requested information.

### The Auditor General's Reliance on Component Auditors

As the auditor of the province's consolidated financial statements, we regard as important the work done by private-sector component auditors, who audit the entities that are consolidated into the government's financial statements. Every year, we issue instructions to specific component auditors in order to obtain information about the audit of their component. We use this information to support our audit opinion on the province's consolidated financial statements. To promote timeliness, we set deadlines for the responses, and emphasize that any significant or unusual events are to be reported to us as early as possible.

During the 2016/17 audit, we experienced significant delays in receiving communication from the component auditor of the Independent Electricity System Operator (IESO). This was concerning because we disagreed with last-minute changes made to the IESO's accounting policies that were significant not only to the province's 2016/17 consolidated financial statements, but also to future reporting in Ontario. Our October 17, 2017, Special Report titled *The Fair Hydro Plan: Concerns About Fiscal Transparency, Accountability and Value for Money* highlighted that these changes were made because they were integral to the accounting and financing structure designed under the Fair Hydro Plan to not show the financial impact of the rate reduction in the province's annual results and net debt.

### Increasing Debt Burden

The province's growing debt burden also remained a concern in 2016/17, as it has been since we first raised the issue in 2011. We focused on the critical implications of the growing debt for the province's finances. We maintained the view that the government should provide legislators and the public

with long-term targets for addressing Ontario's current and projected debt sustainability, and we reaffirmed our recommendation that the government develop a long-term debt-reduction plan to reduce interest expense, ensuring more dollars go toward government programs.

### Ontario Pre-Election Report

The *Fiscal Transparency and Accountability Act, 2004* (Act) requires that, among other things, the government file a regulation to communicate if and when it will release a Pre-Election Report on Ontario's finances in advance of a provincial election. The purpose of the Pre-Election Report is to provide the public with detailed information to enhance its understanding of the province's estimated future revenues, expenses, and projected surpluses or deficits for the next three fiscal years. Under the Act, the Auditor General must review the report to determine whether it is reasonable, and release an independent report describing the results of her review. In our *2017 Annual Report*, we raised a concern that the change of fixed election dates from the fall to the spring could pose time constraints for completing our work in time for the general election on June 7, 2018, especially given that the government had not yet filed a regulation to indicate its intention to release a Pre-Election Report.

We made 10 recommendations, consisting of 14 actions needed for improvement.

## Status of Actions Taken on Recommendations

We conducted assurance follow-up work between April 1, 2019 and October 31, 2019, and obtained written representation from the Treasury Board Secretariat and the Ministry of Finance that, effective November 8, 2019, they had provided us with a complete update of the status of the recommendations we made in the *2017 Annual Report*.

## Discussion of the Accounting Treatment of a Pension Asset

### Recommendation 1

*We recommend the government record valuation allowances to offset the net pension assets it has recorded from the Ontario Teachers' Pension Plan and the Ontario Public Sector Employees' Union Pension Plan until such time as it obtains formal written authorization from their pension plan co-sponsors that they are able to lower minimum contributions or withdraw surpluses from the pension funds within the next 12 months.*

**Status: Fully implemented.**

#### Details

As of March 31, 2017, the government reported net pension assets from the Ontario Teachers' Pension Plan (OTPP) of \$11.511 billion (2015/16—\$10.147 billion) and from the Ontario Public Sector Employees' Union Pension Plan (OPSEUPP) of \$0.918 billion (2015/16—\$0.838 billion), for a total of \$12.429 billion (2015/16—\$10.985 billion). A full valuation allowance against the pension assets should have been recorded in order to comply with Canadian PSAS. Recording a full valuation allowance reduces the net pension asset reported on the consolidated statement of financial position by \$12.429 billion (2015/16—\$10.985 billion), resulting in a net pension liability of \$1.396 billion (2015/16—\$1.673 billion).

In the province's consolidated financial statements for the year ended March 31, 2018, the province recorded a valuation allowance to offset the net pension assets it has recorded from the OTPP and the OPSEUPP.

## Inappropriate Consolidation of the IESO's Market Accounts

### Recommendation 2

*We recommend that the government remove the Independent Electricity System Operator's Market Accounts from the province's consolidated financial statements.*

**Status: Fully implemented.**

#### Details

The province inappropriately recorded market accounts that do not meet the Canadian PSAS definition of assets and liabilities in the province's consolidated financial statements for the 2016/17 fiscal year.

For the province's consolidated financial statements for the year ended March 31, 2018, the government corrected this situation and removed the Independent Electricity System Operator's market accounts from the province's consolidated financial statements.

## The Reasons for the Other Matter Paragraph

### Recommendation 3

*We recommend the government follow the accounting standards established by the Public Sector Accounting Board and the province's historical accounting precedent, and implement the recommendations in the Special Report issued by our Office and tabled in the legislature on October 17, 2017, titled The Fair Hydro Plan: Concerns About Fiscal Transparency, Accountability and Value for Money, as follows:*

- *record the true financial impact of the Fair Hydro Plan's electricity rate reduction on the province's budgets and consolidated financial statements;*

**Status: Fully implemented.**

#### Details

Under the Fair Hydro Plan, the prior government created a complicated structure where the shortfall of funds between the amounts owed to the energy generators and paid by the local distribution companies was being funded by debt incurred by a trust under Ontario Power Generation. This structure was put in place to try to keep the debt off the books of the province and not negatively impact the annual bottom line in the province's consolidated statement of operations.

The province's consolidated financial statements for the year ended March 31, 2018, appropriately reported the debt and deficit of the Fair Hydro Plan. The *Fixing the Hydro Mess Act, 2019*, which received Royal Assent in May 2019, winds down the financing structure established under the Fair Hydro Plan by preventing any further issuance of debt through the inappropriate Fair Hydro Plan structure after November 1, 2019.

- *use a financing structure to fund the rate reduction that is least costly for Ontarians.*

**Status: Fully implemented.**

#### Details

According to our findings in the Special Report titled *The Fair Hydro Plan: Concerns about Fiscal Transparency, Accountability and Value for Money*, the Financial Accountability Officer estimated that the Fair Hydro Plan would have cost the province up to \$4 billion more in interest costs than if the province borrowed the funds directly through the Ontario Financing Authority.

The province corrected the financing structure so that the costs of the rate reduction will be cheaper for all Ontarians.

## The Government's Use of External Consultants

### Recommendation 4

*The Office of the Auditor General is appointed under the Auditor General Act as the auditor for the consolidated financial statements of the province of Ontario. We recommend that the Treasury Board Secretariat:*

- *proactively supply copies to the Auditor General of all contracts it enters into for accounting advice and opinions in order to ensure that our Office is aware of the work the advisors are performing, can assess significant issues in a timely manner, and can determine their impact on the province's consolidated financial statements and our annual audit;*

**Status: Fully implemented.**

#### Details

The interests of the Treasury Board Secretariat, the Ministry of Finance and the Office of the Auditor General are best served when there is full disclosure on the intent and use of external advisors. For this reason, any work performed by external advisors in formulating an accounting position should be shared with the Office of the Auditor General as soon as possible, as part of the audit of the consolidated financial statements.

In the 2016/17 and 2017/18 fiscal years, during the audit of the province's consolidated financial statements, our Office requested that the Treasury Board Secretariat provide us with copies of contracts relating to any advisors it uses for accounting advice and opinions. The Treasury Board Secretariat provided our Office with three contracts for advisors it engaged for accounting advice in 2016/17 and two additional contracts in 2017/18. These advisors provided advice and guidance to supplement the Controller Division's internal analysis of significant accounting issues.

- *build into its contracts with external advisors the requirement that the advisors engaged to provide accounting advice and opinions that affect the consolidated financial statements notify our Office of their engagement as required under the Code of Professional Conduct of the Chartered Professional Accountants of Ontario.*

**Status: In the process of being implemented by December 1, 2020**

#### Details

The Secretariat has agreed to request its external advisors—engaged to provide accounting advice and/or opinions relating to our Office's audit of the province's consolidated financial statements—to notify the Office of the Auditor General of their engagement, as required under the Code of Professional Conduct of the Chartered Professional Accountants of Ontario. In this regard, the Secretariat has incorporated this request into new contracts with external advisors. The Secretariat is

developing a process for other ministries and agencies to request that their external advisors notify us as well.

The province will review and consider updates to existing directives, policies and contract templates over the next 12 months to facilitate the implementation of the recommendation across ministries, agencies and the broader public sector. Ministries and agencies attest through the annual Certificate of Assurance process that they have disclosed all external consulting arrangements.

## The Role of the Group Auditor and the Component Auditor

### Recommendation 5

We recommend that the Independent Electricity System Operator (IESO), an “other government organization,” use the Canadian Public Sector Accounting Standards (PSAS) in the preparation of its financial statements. Specifically, it should:

- remove market accounts recorded on its financial statements;

**Status: Fully implemented.**

#### Details

The IESO inappropriately recorded market accounts that do not meet the Canadian PSAS definition of assets and liabilities in its financial statements for the year ended December 31, 2016, and December 31, 2017.

In its financial statements for the year ended December 31, 2018, the IESO corrected this situation and appropriately retroactively adjusted its 2016 and 2017 financial statements to remove the market accounts.

- discontinue the inappropriate use of rate-regulated accounting in the preparation of its financial statements.

**Status: Fully implemented.**

#### Details

The IESO inappropriately used rate-regulated accounting in its financial statements for the year ended December 31, 2016 and 2017. In its financial statements for the year ended December 31, 2018, the IESO corrected this situation and retroactively adjusted its 2016 and 2017 financial statements to reverse the use of rate-regulated accounting.

*To ensure that the members of the Legislative Assembly receive financial information on the operations of the IESO prepared in accordance with Canadian PSAS, the Office of the Auditor General will conduct an attest audit of the December 31, 2017, financial statements of the IESO as permitted under the Electricity Act, Subsection 25.2(2), which states: “The Auditor General may audit the accounts and transactions of the IESO. 2014, c. 7, Sched. 7, s. 3 (1).”*

**Status: Fully implemented.**

#### Details

We performed a special audit of the IESO’s December 31, 2017, financial statements and were required under Canadian Auditing Standards to issue a denial of opinion because the IESO refused to provide us with written acknowledgement of its roles and responsibilities with respect to our audit (while stating in correspondence that they were co-operating) and would not sign a management representation letter confirming that it had provided us with all relevant information that may affect the financial statements.

Subsequently, the IESO appointed us as the attest auditor for its financial statements for the year ending December 31, 2018. We received all the information required by Canadian Auditing Standards and issued an unqualified opinion.

## Legislated Accounting Standards

### Recommendation 6

We recommend the government follow the accounting standards established by the Public Sector Accounting Board, rather than using legislation and regulations to prescribe accounting treatments.

**Status: Little or no progress**

### Details

The prior government introduced legislation to facilitate the use of specific accounting practices that may not be consistent with Canadian PSAS.

It is important that Ontario prepare its financial statements in accordance with generally accepted accounting standards, specifically those of Canadian PSAS, in order to maintain its financial reporting credibility, accountability and transparency.

At the time of our follow-up, the province indicated it was committed to preparing its financial statements in accordance with Canadian PSAS in order to provide high-quality financial reports that support transparency and accountability in reporting to the public, the Legislature and other users.

However, the province has no requirement to comply with Canadian PSAS. We continue to believe that this recommendation should be implemented and that the province should comply with Canadian PSAS rather than retaining legislation to prescribe accounting treatments.

## Ontario's Debt Burden

### Recommendation 7

*We recommend that in order to address the province's growing total debt burden, the government work toward the development of a long-term total-debt reduction plan linked to its target of reducing the net debt-to-GDP ratio to its pre-recession level of 27% as measured using proper accounting for net pension assets and the projected costs of the Fair Hydro Plan. The government should also discuss publicly how it plans to pay down the debt.*

**Status: No longer applicable.**

### Details

In the province's 2017 budget, the previous government set a target net debt-to-GDP ratio of 27% and then removed this target in its 2018 budget. In its 2019 budget, the current government included a commitment to reduce Ontario's net debt-to-GDP ratio by the 2022/23 fiscal year to less than the Independent Financial Commission of Inquiry's

forecast net debt-to-GDP ratio for the 2018/19 fiscal year of 40.8% of GDP. The province has yet to fully analyze long-term debt sustainability and establish long-term net debt-to-GDP targets to manage debt based on an analysis of future debt sustainability.

## Earlier Finalization of the Province's Consolidated Financial Statements

### Recommendation 8

*We recommend that the Office of the Provincial Controller undertake thorough planning involving all stakeholders, including Treasury Board Secretariat, ministries and provincial government agencies, to identify the barriers and key areas to be addressed to achieve earlier finalization of the province's consolidated financial statements, including the estimation risks associated with corporations tax and personal income tax revenues.*

**Status: In the process of being implemented.**

### Details

The Treasury Board Secretariat and the Ministry of Finance are supportive of the timely delivery of the Public Accounts. The Office of the Provincial Controller is communicating with the Office of the Auditor General to identify audit issues early and to ensure that stakeholders are engaged in discussions regarding risks and resolution. The Office of the Provincial Controller will continue to collaborate with the Office of the Auditor General to support the timely delivery of the Public Accounts.

The Treasury Board Secretariat and the Ministry of Finance are not yet able to move up the timelines for releasing the Public Accounts as the province is dependent on the receipt of taxation information from the Canada Revenue Agency, which it does not receive until mid-July each year.

While the province has made progress on the implementation of this recommendation, it is unable to determine a date by which the recommendation will be implemented.

## The Affordability Fund Trust

### Recommendation 9

*We recommend that the government avoid establishing arm's length trusts in order to record an expense in its consolidated financial statements before it is necessary, given that it loses the ability to ensure that funds are ultimately provided to the appropriate beneficiaries.*

**Status: Fully implemented.**

### Details

By establishing a non-controlled trust (also known as an “arm’s length” trust), the province can record the full amount transferred to the trust as an expense in the year transferred but it loses its ability to ensure the funds were provided to the appropriate beneficiaries and that value for money was obtained. Without the trust, the province would record the expense when the funds are distributed to the beneficiaries.

Since 2017, there have been no additional payments made to the Affordability Fund Trust. One other non-controlling trust was set up in March 2018 related to the Grassy Narrows First Nations and Wabaseemoong Independent Nations, but no other non-controlled trusts have been set up subsequently.

## Auditor General Review of the 2018 Pre-Election Report on Ontario’s Finances

### Recommendation 10

*We recommend that the government publicly communicate if and when it will file a regulation as outlined under subsection 10(1) of the Fiscal Transparency and Accountability Act, 2004 confirming that the government will release a Pre-Election Report and the timelines for release of the Report that will be subject to our review under the Act.*

**Status: Fully implemented.**

### Details

In May 2019, the province passed the *Fiscal Sustainability, Transparency and Accountability Act, 2019*, which replaced the *Fiscal Transparency and Accountability Act, 2004*. Among the changes, the *Fiscal Sustainability, Transparency and Accountability Act, 2019*, now requires the government to release, in a fixed election year, a pre-election report based on its latest budget report, without the need to file a regulation first. In this way, timelines for release of the pre-election report and its review by the Auditor General should be well known going forward.