

REPORT HIGHLIGHTS

October 30, 2008

Observations on Financial Reporting: Audit Findings Report on the 2007/08 Summary Financial Statements

Introduction

The Public Accounts report annually on the financial performance of the government of British Columbia. Its main focus is the Summary Financial Statements, on which the Auditor General provides an audit opinion. Each year the Auditor General comments on the quality of government's financial reporting to assist it in meeting a stated commitment to improvement.

This report informs legislators and the public about the Auditor General's opinion of government's 2007/08 Summary Financial Statements, and discusses significant findings relating to the audit. It is also intended to encourage improved practices in financial reporting and management.

This report has also developed to focus on a broad range of governance, financial management and other issues relevant to the government organizations included in the Summary Financial Statements.

Overall conclusions and key findings

Audit reservations related to the 2007/08 Summary Financial Statements

During our audit of the Summary Financial Statements, we discussed a number of significant issues with government, many of which were satisfactorily resolved. However, government chose not to adjust some of these items in its financial statements and notes. Therefore, in the Auditor General's opinion, six reservations were expressed for departures from Canadian Generally Accepted Accounting Principles. And, for one material balance in the Summary Financial Statements, the Auditor General was not able to obtain sufficient, appropriate audit evidence to determine the reasonableness of government's estimate, resulting in a scope limitation.

There are seven reservations:

1. Resource roads – limitation on the audit scope
2. No separate disclosure of liabilities related to leased tangible capital assets
3. Land used for highways not properly disclosed
4. Oil and natural gas producers royalty credits inappropriately netted from revenues
5. No provision for deep-well credits
6. Inadequate disclosure of a First Nation loan guarantee amount
7. Failure to recognize a portion of a First Nation settlement

An unreserved, or “clean”, audit opinion does not signify that a set of financial statements are free of all possible errors or have lesser quality disclosures of financial results or condition. However, while financial statements with audit reservations do not necessarily indicate serious problems, they should also not be taken lightly. While these reservations are of concern, the Summary Financial Statements are, in the Auditor General’s opinion, otherwise fairly presented according to Canadian standards.

Other future significant accounting issues

In our audit of the Summary Financial Statements, we did not consider the impact of government’s accounting treatment on First Nations settlements material enough to include a reservation in the Auditor General’s opinion. However, it is possible that the amounts involved in these settlements will be material in the future. We also believe that this is an area where government’s commitment to transparency should be improved in its disclosure of these transactions.

Another accounting issue we discuss is government’s accounting for, and recognition of, inherited Crown land when it is to be sold or given away. We disagree with how government accounts for these transactions and have made several recommendations in this area. We believe that these transactions, some of which are also related to First Nations issues, may be material in the future, and if not accounted for correctly, may result in future audit reservations.

Other audit findings reported to government organizations

The Summary Financial Statements brings together the financial performance of 148 separate government organizations and the Consolidated Revenue Fund. In conducting these individual audits, internal controls over financial disclosure, financial management and governance are considered, and weaknesses are brought to management’s attention. Management must then weigh the cost of implementing the recommended improvement against the benefits.

We reviewed over 350 issues from entities in the government reporting entity, the ministries and the Office of the Comptroller General. Of those entities reviewed, over 60% had findings. Included in these findings were the following categories:

- Capital asset policies.
- Assurance for use of service providers.
- Account reconciliations.
- Inventory management procedures and the accuracy of data.
- System documentation and controls.
- Segregation of duties.

To help organizations identify and mitigate risk we have summarized our major findings highlighting those areas having the greatest potential risk and impact. Our findings are presented so entities can examine them with an eye to self-improvement for government organizations.

Progress on our prior year recommendations

Government has made improvements in disclosure in the use of estimates, updating estimates of long-term liabilities and consistent use of interest capitalization. Also, in 2007/08, some resource roads not previously capitalized have been.

Looking forward

New financial reporting standards

Canada has announced that Canadian private sector accounting standards will converge with international ones by 2011. Although no decision has been yet been made with regards to all public sector accounting standards, there are many entities included in the Summary Financial Statements that must use private sector standards, and will have to adopt the new international standards.

There will be considerable additional work and complexity in the consolidation process at the summary level with the adoption of these new international standards. We believe that government could reduce these impacts by being more proactive in setting a general reporting framework for Internal Financial Reporting Standards (IFRS) in the public sector.

Recommendations to improve future financial statements

To assist government's ability to improve the quality of its financial statements in future years, and in addition to our recommendation relating to audit reservations, we make several recommendations in the following areas:

- Review of accounting policy and guidance regarding measurement and recognition of First Nations settlement costs;
- Treatment, disclosure and valuation of inherited Crown lands;
- Improved assessment and disclosure of contractual obligations; and
- Improved segmented reporting disclosure.

Overall

Government's Summary Financial Statements are acceptable, but it could be better. Most of the issues raised in this report could easily be resolved.

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A copy of the full report is available on our website at: www.bcauditor.com