

**2004 Report of the Auditor General
to the Northwest Territories
Legislative Assembly**

September 22, 2004

The Honourable Paul Delorey, MLA
Speaker of the Northwest Territories
Legislative Assembly
Legislative Assembly Building
P.O Box 1320
Yellowknife, NWT
XIA 2L9

Dear Mr. Delorey:

I herewith transmit my Report, in English, to be tabled before the Legislative Assembly in accordance with the provisions of Section 30(2) of the Northwest Territories Act, R.S., c.N-22, s.1.

The report deals with "Other Matters" arising from our audit of the financial statements of the Government of the Northwest Territories for the years ended March 31, 2002 and 2003 that, in my opinion should be brought to the attention of the Legislative Assembly. The report also includes our recommendations and related management responses.

Yours sincerely,

Sheila Fraser, FCA

Encl.

Contents

2004 Report of the Auditor General to the Northwest Territories Legislative Assembly

Chapter		Page
	Introduction—About the Audit and the Office of the Auditor General of Canada	2
1	NWT Housing Corporation—Shipment of Unassembled Housing Units to Alaska	6
2	Loan Guarantees	11
3	Revenue and Recoveries	
	Recovery of Indians and Inuit hospital and medical care costs—Follow-up	21
	Projects done on behalf of others, funding, authority and administration	
	Risk of errors in Formula Finance Grant	
	Revenue fluctuations—Corporate income taxes	
4	Land Ownership—Transfers from Canada	30
5	Protecting The Environment—Clarifying Responsibilities	36
6	Other	39
	Division of the Northwest Territories Power Corporation	
	Services and facilities provided without charge to government agencies	
	Consolidated budget	
Appendix I	Our People	47

Introduction

About the Audit and the Office of the Auditor General of Canada

Our vision

The Office of the Auditor General (the Office) is an independent audit office serving the Legislative Assembly and the well-being of people of the Northwest Territories.

We promote

- accountable government,
- an ethical and effective public service,
- good governance,
- sustainable development, and
- the protection of the Northwest Territories' legacy and heritage.

We do this by

- conducting independent audits and studies that provide objective information, advice, and assurance to the Legislative Assembly, the Government, and the people of the Northwest Territories;
- working collaboratively with legislative auditors, federal and

territorial governments, and professional organizations; and

- providing a respectful workplace in which our diverse workforce can strive for excellence and realize their full career potential.

Our mandate

In accordance with the *Northwest Territories Act*, section 30(1), we audited the accounts and financial transactions of the Government of the Northwest Territories (the Government) to express an opinion on that government's consolidated financial statements for the years ended 31 March 2002 and 31 March 2003.

Our audits included reviews of certain operating, legislative and financial control systems and financial management practices, with detailed tests as we considered necessary. At the conclusion of our audits, we issue our opinions, which are attached to the respective financial statements.

This *Report of the Auditor General to the Legislative Assembly of the Northwest Territories*, also known as the Report on Other Matters (ROM), is part of our audit. In accordance with the *Northwest Territories Act*, section 30(2), the Auditor General is to report on any “other matters” arising from the audit that she feels should be communicated to the Legislative Assembly. Individually or collectively, they have not generally been significant enough to require a reservation of opinion in our Auditor’s Report.

Each of the significant matters reported in this report was examined in accordance with generally accepted auditing standards; accordingly, our examination included such tests and

other procedures as we considered necessary.

Our audit work

This report contains comments on items that we believe will be of interest to members of the Legislative Assembly; it also contains our recommendations and management’s responses, where appropriate.

We issued unqualified audit opinions on the financial statements of the Government of the Northwest Territories for the years ended 31 March 2002 and 31 March 2003.

We also issued unqualified audit opinions on the following Government entities in accordance with the Northwest Territories’ *Financial Administration Act*, section 99:

Entities	Years ending
Aurora College	30 June 2002 30 June 2003
Northwest Territories Power Corporation	31 March 2002 31 March 2003
Northwest Territories Housing Corporation	31 March 2002 31 March 2003
Northwest Territories Development Corporation	31 March 2002 31 March 2003
Northwest Territories Business Credit Corporation	31 March 2002 31 March 2003
Workers’ Compensation Board of Northwest Territories and Nunavut	31 December 2001 31 December 2002

We also issued unqualified audit opinions on the following Government entities in accordance with ministerial appointments:

Entities	Years ending
Northwest Territories Liquor Commission	31 March 2002 31 March 2003

Other audit work for the Government of the Northwest Territories

At the request of the Department of Health and Social Services, we carried out audit work on the health indicators included in the Government's publication *The Report to Residents of the Northwest Territories on Comparable Health and Health System Indicators* (September 2002). This publication reported health indicators for the territory as agreed in the communiqué on health issued by the first ministers in September 2000, in which they had agreed to provide clear accountability reporting to Canadians. The first ministers had directed the ministers of Health to provide comprehensive and regular public reporting. They had also been directed to collaborate on the development of a comprehensive framework using jointly

agreed-upon indicators comparable across Canada addressing health status, health outcomes, and quality of service. This was the first report on the 14 indicator areas for the Northwest Territories.

Reporting and management comments

Our Office policy is that audit observations and recommendations be referred to the management of the audited organizations for comment. Where appropriate, the Office obtains management's written responses to recommendations contained in our reports.

We provided our draft report to the Office of the Comptroller General, departments, and territorial corporations, where appropriate. Management responses from the departments and territorial corporations are included in the relevant chapters.

Our thanks

Management provided explanations, information, and full access to all documents requested during our audits. We thank the staff of the Government of the Northwest Territories and its entities for their co-operation.

For comments or questions on this report, please contact Roger Simpson at (780) 495-2028.

Chapter 1

NORTHWEST TERRITORIES HOUSING CORPORATION SHIPMENT OF UNASSEMBLED HOUSING UNITS TO ALASKA

1.1 The original purpose of the Northwest Territories Housing Corporation was to provide social housing to Northwest Territories residents. However, the management of the Corporation has interpreted the legal authorities included in the *Housing Corporation Act* to allow it to undertake different ventures.

1.2 In our September 2002 Report, we noted our concerns that the Corporation may have exceeded its mandate and authority by acting as a general contractor in the construction of a seniors' complex in Alaska. It seems clear, reading the legislation that established the Corporation that the Corporation was created to address housing needs of residents of the Northwest Territories. Paragraphs 1.15 to 1.19 give further details about our concerns raised in our September 2002 Report on this issue.

1.3 In this report, we note our concerns about the attempted sale of unassembled housing units in Alaska. The

venture was unsuccessful and exposed the Corporation to losses and unnecessary risk. Any time a venture fails, it is important to investigate why and to ask what should be done differently in the future.

1.4 The Corporation tried to sell housing units in Alaska on which it lost money. In our view, management failed to follow certain basic accepted business practices that could have reduced its risk. As noted in previous reports, we question whether the Corporation actually has a mandate to carry out activities in other jurisdictions. The Corporation's continued attempt to sell these units overlapped a meeting of the Standing Committee on Accountability and Oversight (the Standing Committee) that discussed other activities for which the Corporation did not have a clear mandate. At this meeting, management committed not to undertake such ventures in the future without a clear legislative framework.

This venture:

1.5 In August 2001, the Corporation shipped nine unassembled housing units to the State of Alaska. This was done based on a verbal agreement with municipal authorities from a village in Alaska, that the village would purchase the units. The Corporation shipped these units without obtaining a written contract or a deposit. Ultimately, the village only purchased one unit, in June 2002.

1.6 The eight unsold housing units remained in Alaska sitting in crates at an outdoor storage area, until the late summer of 2003. The eight units cost the Corporation \$800,000 for components and shipping costs to Alaska, plus storage, but this amount did not include overhead costs.

1.7 The Corporation was unable to sell the eight units, which were subsequently shipped to Tuktoyuktuk, NWT, at an additional cost of \$250,000. As of November 2003, the Corporation management had not yet decided what to do with the units. These units are generally more expensive than most public housing units in the NWT, because most of them are above the basic standards used for NWT public housing.

1.8 The Corporation could have reduced its risks and losses if its management had a signed sales agreement before shipping the houses to Alaska and had taken a deposit.

1.9 The Corporation also exposed itself unnecessarily to risks in other ways on this venture, for example:

- the Corporation had no storage agreement with the Alaska warehouse between August 2001 and June 2002. Therefore, the legal responsibilities of both parties would not have been clear if problems (for example, theft, and fire) had arisen.
- the housing units were designed by the Corporation above the standards used for public housing in the Northwest Territories so the units could be readily sold in the marketplace. However, it was not certain if, before being shipped, the units would even have met the building codes in Alaska. Even if the Corporation had found a potential buyer, this possible failure to meet the codes could have prevented the sale.

1.10 At this time some units are damaged and some materials are missing. The units are not insured.

1.11 This venture was not successful in a number of ways. Furthermore, the money spent on the units and the additional costs of shipping could have been used to build houses for NWT families.

1.12 The Northwest Territories Housing Corporation should develop and follow standard procedures when undertaking the sale of housing units. Examples of these standard procedures include:

- **Having a sales agreement before shipment.**
- **Having a lease agreement for the storage of the units.**
- **Preparing a cost benefit analysis before entering into the arrangement.**

Corporation's response:

The Corporation will ensure that the following sound business practices are incorporated into future sales and leasing agreements:

- ***Signed sales agreements and deposits to be received before assembling and shipping goods for sale;***

- ***Lease agreements to be established before utilizing storage facilities;***
and
- ***A cost benefits analysis to be undertaken before entering into a sales arrangement.***

Authority

1.13 In Chapter 4 of our September 2002 Report, we made recommendations regarding whether the Corporation's mandate allowed it to undertake activities in Alaska. The same recommendations also apply to the attempted housing sales discussed in this chapter, as these attempted sales did not address housing needs of NWT residents. As mentioned in our previous Report it seems clear, reading the legislation that established the Corporation: the Northwest Territories Housing Corporation was created to address the housing needs of residents of the Northwest Territories.

1.14 These units were shipped prior to our September 2002 Report but were not covered in that Report. Our recommendations along, with the Corporation's response, and the Standing Committee's corresponding recommendation were as shown:

Our previous recommendations, management responses, and the Standing Committee's recommendations

1.15 The Legislative Assembly, and in particular the Executive Council, is ultimately responsible for all areas of management of the Government, including setting policy and managing finances. The activities of Crown corporations do affect the activities of the government as a whole; any intended activities that put the GNWT at risk, such as taking on debt, or exceeding the mandates of the Crown corporations, should be communicated to the Legislative Assembly in an appropriate manner. For example, relying on implied authorities is not, in our opinion, a good substitute for specific authority requests, discussions and approval by the Legislative Assembly.

1.16 For any proposed new lines of business, the Corporation should ensure that it has legal capacity to do work under its own Act. When relying on the authority contained in its legislation to carry out other duties that may be assigned to it, the Corporation should ensure that the duties have indeed been assigned to it by the Legislative Assembly.

The Corporation's management response:

1.17 It is the Corporation's contention that the review and approval mechanisms established by the Government sufficiently address the concern that the Legislative Assembly may have not been properly informed on this matter. The Corporation identified this activity as one of its four main business areas in its 2000–2001 Business Plan. The Standing Committee on Social Programs, the Minister and the FMB approved the Business Plan.

1.18 The Corporation had political support to proceed with its activities in Alaska and the NWT Housing Corporation Act does not specifically limit the activities of the NWTHC to the NWT. It has however decided to take a cautious approach and will not pursue any further general contracting activities in other jurisdictions without a clear legislation framework to support its activities.

Accountability and Oversight Committee recommendation:

1.19 Committee members recommended the Corporation go back to the Financial Management Board or the Executive Council to clarify its mandate. Many Committee members noted that the Corporation had clearly moved beyond its original social housing obligations to include other activities.

1.20 The Corporation shows the costs of these units at almost \$1 million, including the shipping costs. Given the missing parts and reported damage to some of the crates, it is not clear yet what the ultimate loss will be.

1.21 The Northwest Territories Housing Corporation should not pursue any further activities in other jurisdictions without a clear legislative framework to support its activities.

Corporation's response:

As previously stated no future business deals will be considered with other jurisdictions unless we have a clear mandate from the Government of the Northwest Territories.

Chapter 2

LOAN GUARANTEES

Background ¹

2.1 The Government of the Northwest Territories gave loan guarantees to three companies in the diamond industry. These guarantees allow businesses to obtain private financing that might not otherwise be available. The maximum amount that was originally guaranteed under the three guarantees was \$24.2 million. The Government paid out \$2.6 million to Deton'Cho Diamonds Incorporated, as the bank had called in its loan. A subsequent agreement was reached

with the Deton'Cho Corporation, a different company, which was a guarantor to the Government in the original agreement, to recover the \$2.6 million principal amount over an extended period.

2.2 The two remaining guarantees have allowed Sirius Diamonds Ltd. And Arslanian Cutting Works (NWT) Ltd. to borrow over \$17 million from their bankers up to 31 March 2003, as disclosed in note 18b, to the 2003 Public Accounts (Exhibit 2.1).

Exhibit 2.1

Amount of money guaranteed by the Government of the Northwest Territories and the operating line of credit balances for two diamond companies

Company	As at 31 March 2003	
	Maximum guaranteed	Operating line of credit balances
Sirius Diamonds Ltd.	\$ 10,000,000	\$ 7,960,000
Arslanian Cutting Works (NWT) Ltd.	9,200,000	9,050,000
Total	\$ 19,200,000	\$ 17,010,000

¹ The Financial Management Board Secretariat co-ordinates providing loan guarantees to the diamond industry for the Government. The Department of Resources, Wildlife and Economic Development is also heavily involved.

2.3 Loan guarantees can be a useful way to encourage economic development. They can be attractive tools for governments, as economic activity usually occurs quickly after the loan guarantee is provided. Guarantees do not cost the Government any money up-front when they are given, unlike contributions or loans. But, if the company later defaults on its loans, the banker requires the Government to pay off the company's guaranteed borrowings.

2.4 Loan guarantees support businesses that banks would often consider too risky to lend to, without government backing. However, these loan guarantees do come with a risk. If the business fails, it can mean a significant cost to a government.

How can the risk be minimized?

2.5 The Government must do its homework carefully to satisfy itself that it is not assuming too much risk, and the business has sound prospects. This is usually called "acting with due diligence". It requires staff to carefully analyze all aspects of the business including the following.

- Does the business have access to a supply of materials?

- Are there markets available, where the finished products can be sold at a profit?
- Does the business have people with the right skills to do the work?
- Can the business find and lease appropriate premises with security?
- Is the management in charge of the business knowledgeable?

These are examples of the variety of other important questions that should be asked. The answers have to be weighed against the potential benefits to the economy, such as jobs, economic spin-offs, skills development, and potential tax revenues. In other words, the due diligence process should do as complete a job of assessing the risks of the business, as if it was preparing the analysis for a government loan to the business.

Deton'Cho Diamonds Incorporated (the company) had its \$2.6 million loan called

2.6 When it became clear that a commercial diamond industry was possible in the NWT, Government help to local businesses became a priority. Deton'Cho Diamonds Incorporated was new, and was 50 percent owned by a local First Nation Corporation and 50 percent owned by other interests, including the person who became the production manager. The company

received a government loan guarantee of up to \$5 million, and this allowed it to access a line of credit from a bank. The company used \$2.6 million on its line of credit from the bank, during the 2002 fiscal year.

2.7 After a short operating period, the company's cutting and polishing operations were shut down in July 2002. Government staff later indicated to us that the company lacked experienced staff time to manage the production of the diamonds and to market them. Yet, heavy reliance on one individual for each of these two tasks were two of the risks that had been identified in the due diligence process. Although these risks had been identified, the Government staff, which analyzed the risk factors before approving the loan guarantee, concluded the managing and marketing team was sufficient. The bank called the loan, and the Government paid out its loan guarantee for \$2.6 million in July 2002.

2.8 Exercising due diligence means government employees must know and obey environmental laws and regulations, exercise caution, prepare for risks that a thoughtful and reasonable person would foresee and respond to risks and incidents as soon as practicable. In this case, the Government had spent a lot of time going through the process of due diligence. We

would have expected this process to identify all significant risks and make sure that the company had a sound plan to mitigate or minimize them. Yet the company soon started building up losses. When we initially reviewed the financial statements of the company, we wondered why the due diligence process had not led to solutions to these identified risks. The due diligence team had identified key risks but had rationalized that things would work out well. This points out a fundamental problem, in which a well-designed process can work to identify the risks, but decisions made by people may not give appropriate weight to the identified risks. This can result in a poor decision that costs the Government money.

Subsequent government action

2.9 Note 8 to the 2003 Public Accounts includes a partial description of later events. When the borrower defaulted, the Government paid up under the guarantee, through its agents, and took over the shares in the company. It then sold the shares for \$2.6 million to a First Nation corporation that was related to the First Nation Corporation that had owned 50 percent of the company. This is the amount that the Government had to pay to the bank under its loan guarantee. The new owner will pay for the \$2.6 million shares in

20 equal, interest-free, yearly instalments. If these instalments are paid as scheduled, the Government will get money back, but in tomorrow's discounted dollars, and at a significant cost in lost interest. (As an example, using a modest discount rate of 4 percent, the money to be collected will be approximately \$1,800,000, only 70 percent of the amount the Government paid out). Just for the 2003 fiscal year, the Government lost interest of approximately \$95,000.

2.10 While the precautions that the Government had built in to the contract for the loan guarantee should reduce its losses, it also provided funding to the company through other programs, and the total cost of this failed business to the Government is not known with certainty at this time.

The due diligence process used

2.11 We have concerns about this process, especially since the company's actual financial results bear little or no resemblance to the projected results that the Government used in its decision to approve the loan guarantee. The figures proposed by the company (and accepted by the Government) look nothing like the actual results for its first and second full years of operation. In the first year, the

company projected sales of \$16 million and a profit of \$1.6 million; however, it only sold \$700,000 in products and lost a total of \$1.2 million. In the second year, the projected sales were \$24 million, but the company realized only \$2.7 million. The projected profits of \$3.3 million did not appear, and the company lost \$1.7 million. The total sales projected over its first two full years of operation were \$40 million, yet in actual fact, the company sold less than \$3.5 million in that period.

2.12 We examined the review team's documentation for the company's project. The Government's due diligence process included many of the steps that such a process should include. It did the following:

- produced detailed criteria and business plan outlines against which to measure diamond processing proposals;
- formed a committee and sub-committee to review the proposal;
- hired an outside diamond expert, with over 20 years experience in the diamond industry to review the initial business plan. He provided detailed comments on the plan in key areas including:
 - production,
 - rough to polish conversion,
 - training program,
 - receivables and payables,

- marketing,
- manufacturing facilities and equipment,
- business development plan, and
- management.

2.13 A second consulting firm reviewed the business plan without the financial analysis, and investigated both the company and its principals.

2.14 Yet, even with these steps, the question becomes “how did the actual results fall so short of those that were projected?”

2.15 Is it due to events that could not have been reasonable foreseen by due diligence? Was there insufficient rigor in the process? Did the plan include overly optimistic assumptions? Were some of the risks discounted in trying to achieve a broader objective? Or were subsequent operations significantly different from the plan, in which case we wonder why Government monitoring did not identify the differences?

2.16 Government staff told us that the poor results were due to the company's experienced staff spending insufficient time in managing diamond production and marketing. Staff also noted that there was no agreement amongst the shareholders

concerning their individual participation. The company's reliance on a few experienced staff in managing diamond production and marketing was a key concern raised by the due diligence team. Another important consideration was that the company was new and had no previous track record. The company and its shareholders noted to us several other reasons for the poor results including the high cost of rough diamonds and shortage of skilled labour.

2.17 In particular, the due diligence team noted that the company planned to rely heavily on one person who would be in charge of the manufacturing side. This person was a part owner in the company, a fact noted by the review committee, which had assessed his connections and prior experience. The other critical person was the marketing manager. The review committee noted that he had no specific experience in selling diamonds but discounted this risk by rationalizing that the production manager's contacts would help to compensate.

2.18 Given that a later explanation for the failure was that the company's experienced staff lacked time to manage production and market diamonds, we wonder why these important factors were not given more weight in the decision.

Even without the benefit of hindsight, they seem to be large risks.

2.19 We saw little documentation of alternatives to relying so much on the important key person. Alternatives such as hiring in a knowledgeable deputy or partnering with an organization experienced in the diamond industry were not considered necessary during the due diligence process.

2.20 Instead, the review team felt that the company's staff members could have access to a qualified team of consultants, if they needed it. It is not clear if the consultants were ever used or, if used, why they did not compensate for the limited experienced staff with marketing and production experience as the review team originally discussed.

Did the due diligence process minimize the risks too much

2.21 Although the process identified the concerns about heavy reliance on a limited number of individuals, the Diamond Review Committee concluded the management team was capable of successfully implementing the business plan. The consequence was to put millions of Government dollars at risk, based on the skills of a limited number of individuals with diamond marketing and production

experience. This was done without reducing the concentration of risk by bringing in a partner organization with the necessary skill sets.

2.22 An after-the-fact review by a national firm was highly critical of the way this business was run with few if any controls over key aspects. This points to a possible problem with the due diligence process that, in spite of identified risks, rationalized that things would work out well. All this was against the back-drop of a new highly specialized business. As the problems started as soon as the guarantee and loans were approved and proceeded to get worse rapidly, a question that should be asked is whether the due diligence process was handled too quickly and whether or not, the management team took time for a sober second look.

2.23 The company's business plan was changed late in the process. The plan dated 28 February 1999 projected five years of sales and net profits. On 2 March, the plan was revised to show an increase in profits of 34 percent. Later that month, the final profit projection was raised by another 2 percent. Over this short period, the projected loan guarantee that the company requested from the Government was reduced from \$10 million to just one-

half of that to \$5 million. These changes meant that the March revised business plan was very different from the February 1999 plan in several ways.

2.24 The company's December 1998 business plan, containing figures comparable to the February 1999 version, had been reviewed by outside consultants. From the documents we examined, it is not clear whether the March 1999 plans were scrutinized as closely, or even if they were scrutinized at all by independent reviewers.

2.25 Although the March 1999 final plan had detailed figures to support it, we note that the outside expert felt that for the most part the figures in the December 1998 version were also reasonable.

2.26 This begs the question of whether the project really needed more Government financial support as suggested in the original plan to be viable.

2.27 Likely, no one will ever know whether additional funding would have helped the venture to buy sufficient management skills for manufacturing and marketing, especially as these were later given as the reasons for the failure of the venture. These reasons suggest that the company may have been under-financed, forcing management to make poor

decisions. The Government's view is that poor decisions resulted in the company not being able to operate within its financing capacity.

2.28 The Government of the Northwest Territories needs to review all factors that led to the failure of the company to see what lessons can be learned for the future in doing due diligence reviews of high-risk ventures.

Government's response:

The chief factor that led to the failure of Deton'Cho Diamonds Ltd. (DDI) was the company's management and their inability to carry out the business plan as presented in their original proposal.

The GNWT entered into the loan guarantees knowing there were inherent risks. The due diligence review, undertaken prior to approval of the loan guarantees, was thorough and intended to identify and minimize the risks. However, the success of a business plan is highly dependent on the ability of the management team to implement the plan. When assessing a business proposal, extensive reliance is placed on the past experience of the principals who will be involved in the management. Based on the business case presented and the assessment of

the management, a decision was made. Subsequently, there were changes in the management structure that impacted the ability of DDI to implement the business plan.

Subsequent to the review and approval of the initial three northern diamond manufacturers, the Diamond Review Sub-Committee did undertake a review of the process and recommended changes to be implemented in the review of future proposals. This was a new venture for the GNWT from which a number of lessons have been learned which will help to minimize risks in

future ventures. However, issuing loan guarantees to support a new industry is inherently high risk and no amount of due diligence will change this.

Multiple sources of funding

2.29 The venture received financial support from three territorial government programs and three federal government programs, including the loan guarantee by the Government of the Northwest Territories.

2.30 Exhibit 2.2 shows the financing that Deton 'Cho Diamond Incorporated expected would be available according to the business plan.

Exhibit 2.2

Sources of program financing	Amount
Loan Guarantee	\$ 5,000,000
Other GNWT	\$ 1,250,000
Canada	\$ 1,095,123
Equity (non-gov't)	\$ 1,250,000
Bank Mortgage	\$ 1,200,000
	\$ 9,795,123

2.31 The GNWT provided a contribution and a loan totalling \$1,250,000. At 31 March 2003, the Government had provided for a bad debt of \$750,000 against its loan. In 2001, the Government stopped recording interest revenue. In May 2003, one of the guarantors made payments to bring the loan up-to-date.

2.32 When a business receives financial support from multiple programs funded by taxpayers, the amounts and reasons should be reported and be transparent to members of the Legislative Assembly.

2.33 From the perspective of the Government of the Northwest Territories, there can be advantages for leveraging its funding to also attract federal government funds. Some government funding is for targeted areas such as training, and this can lead to multiple funding for particular projects.

2.34 With multiple programs providing funding, the overall risks and costs to the Government are not always clear. By spreading the funding between various programs there is a danger that the Legislative Assembly may not be told the

full potential costs and risks, and that if things go bad, it is difficult to hold any one department responsible.

2.35 The total financial exposure of the Government should be clear regardless of the number of programs funding a particular venture. In analyzing a proposal the Government should consider its overall exposure under various programs.

Government's response:

The Diamond Review Sub-Committee was responsible for the review and assessment of proponents seeking approval as northern manufacturers and government assistance. The sub-committee is comprised of representatives from Resources, Wildlife and Economic Development, NWT Business Credit Corporation, Education, Culture and Employment and the Financial Management Board Secretariat. Each of these departments or agencies was involved in providing assistance to the approved diamond manufacturers through: Business Development Fund contributions; BCC loans; training subsidies; and loan guarantees.

The range of financial assistance, available to northern diamond manufacturers, was disclosed in the GNWT's "Policy Framework on GNWT Support to the Diamond Value Industry", approved by Cabinet in June 1999. The Diamond Review Sub-

Committee was aware of the full extent of government assistance being requested in each proposal and this was disclosed in the final recommendations to the Financial Management Board.

Chapter 3

REVENUE AND RECOVERIES

Recovery of Indians and Inuit hospital and medical care costs— Follow-up

3.1 In our September 2002 Report to the Legislative Assembly, we noted that the federal government owed large amounts to the Government of the Northwest Territories for hospital and medical care costs for Indians and Inuit.

3.2 The territorial Government delivers programs to its qualified residents on behalf of Canada, which is responsible for the costs. For many years it has had to pay for the costs itself and collect later from the federal government. Collection of

the large amounts takes a long time. Meanwhile the territorial Government has to use its own financial resources to finance Canada's federal health program.

3.3 The federal government continues to owe large amounts to the Government of the Northwest Territories for this program; \$34.9 million and \$25.4 million for the years ended 31 March 2002 and 31 March 2003 (see Exhibit 3.1). It can take more than a year for the federal government to pay the amounts owing, making this an expensive type of financing for the territorial Government.

Exhibit 3.1

Amount of money owed by the federal government to the Government of the Northwest Territories by year

	Year owed (\$ millions)			
	2000	2001	2002	2003
Amount owed as at 31 March of each year to the Government of the Northwest Territories	\$26.5	\$19.3	\$34.9	\$25.4

3.4 We have reported this issue before, but have not seen any marked improvement. The federal government will not agree to an interim funding agreement. A yearly agreement provides the contract basis, but hold-ups in signing it cause major delays in collecting the money from the federal government. If the agreement was completed at the beginning of each fiscal year, the territorial Government could make periodic claims and receive 90 percent of the money quickly. However, there is always a delay. For example, the 2002–2003 agreement was not signed until March 2003. The Government of the Northwest Territories spent \$23.2 million for that year, but could not collect its money back for over a year. With a more prompt audit process, it could also collect the remaining 10 percent more quickly. At 31 March 2003, the audit for 2002 year was not complete, and Indian and Northern Affairs Canada still owed the territorial Government 10 percent of the total amount to be paid.

3.5 Given the many demands made on its own limited funds, the collection delays put a burden on the territorial Government.

3.6 The Department of Health and Social Services tried to resolve this problem by formally requesting that Indian and Northern Affairs Canada sign an interim billing agreement, so that the territorial Government could receive at least a portion of its money quickly. INAC declined, stating that the agreement for 2003–04 would be finalized early in 2003–04, which would eliminate the need for an interim billing agreement. In actual fact, the Minister of INAC signed the agreement on 29 September 2003, six months after the start of the year.

3.7 The Department of Health and Social Services plans to complete its claims, and get the claims audit ready more quickly. However, past audits were delayed for various reasons. For example, the one for 2001–2002 was delayed due to problems in determining the costs for physician services in the Northwest Territories. The Department of Health and Social Services has proposed cost solutions to Indian and Northern Affairs Canada that may result in quicker completion of the claims.

3.8 The Department of Health and Social Services should work with INAC to finalize its agreements earlier and ensure that claims are prepared and audited more quickly.

Department of Health and Social Services' Response:

Since the time of the period covered by the Report of the Auditor General we have improved our reporting to INAC to the point where we are current with the submitting of all audited claims.

The only outstanding amount due the GNWT at this time is the 10% hold backs of \$2.3 million and \$2.4 million for 2002-2003 and 2003-2004 respectively. We have recently received notification that the \$2.3 million has been approved for payment. The \$2.4 million will be released when the 2003-20004 audited claim, which is due September 30th, is submitted.

We have signed an agreement with INAC to cover the 2004-2005 year and it has been returned to INAC but, due to the recent election, we do not anticipate it to be signed off there until a new Minister has been appointed. To get an agreement in

place on a timely basis continues to be a problem but both INAC and the Department are working towards expediting it.

Projects done on behalf of others, funding, authority, and administration

What is it and why is this important?

3.9 A significant part of the activity of the territorial Government is delivering projects in the NWT for others, most notably the federal government, and assisting the Government of Nunavut with various transitional arrangements. Most of the contracts are done on a “cost-recovery” basis where direct project costs are payable by the other party. The contracts also allow the GNWT to recover its overhead or administrative costs. In some cases, however, the GNWT does not collect administration costs, which then come out of the GNWT's own funds.

3.10 In the two years that ended 31 March 2003, the Government did \$100 million worth of business, with these types of contracts—not an inconsiderable amount—and obviously of benefit to the economy of the NWT. The territorial Government's Public

Accounts show these contracts as vote 4/5 with matching receipts and payments.

3.11 Over the past few years we have had some concerns about how these projects are managed. In many cases the GNWT has to provide its own working capital for these projects, and the other parties have not, in some cases, reimbursed the GNWT for months or years later. In some cases the reimbursement does not occur until after difficult negotiations are completed. A few years ago, GNWT was not able to recover all the expenses it incurred on one of these projects, resulting in a bad debt to the GNWT of over \$500,000.

3.12 We have three concerns:

- a. A lack of advance financing by the other parties requires the GNWT to provide working capital for projects.
- b. The legislative authority for using GNWT money for these projects is unclear.
- c. The administrative costs incurred by the GNWT may not be

recovered from the other parties as intended.

Types of projects and numbers

3.13 The territorial Government handles over 125 projects and programs on behalf of others. Some of the larger ones involve the following:

- non-insured health benefits,
- Inuvialuit land claim implementation,
- air navigation services,
- exchange of services—Nunavut inmates, and
- labour market development.

3.14 The territorial Government must advance money and then must recover the money for vote 4/5 programs. We have commented above about the delays in receiving federal money for Indian and Inuit health care. The same types of difficulties can be encountered for vote 4/5 programs, particularly the late receipt of cash.

Legislative Assembly authority

3.15 Using funding from the territorial Government to pay the up-front costs of these projects is also a concern from an

authority perspective. The Legislative Assembly does not vote on these expenditures. Arguably, the territorial Government should not be spending this money unless the third party has covered the costs through advances.

Overhead or administration costs

3.16 An ongoing issue is whether the GNWT actually recovers all of its own overhead (or administrative) costs on these projects as intended by the contract with the other party. It is difficult to determine exactly what these costs are and which expenses the contract allows to be reimbursed. The Government does not recover administration costs associated with vote 4/5 projects consistently.

3.17 Also, as the projects are often important to the GNWT for economic or social reasons, the GNWT may determine that, for certain projects, it is not as important for the GNWT to recover administrative costs. Under these circumstances any waived recovery of administration costs should be explicit in the contract.

3.18 In cases where these are waived, the Financial Management Board makes the decision.

Government's response:

A majority of our agreements for projects on behalf of others are with Canada. The ability of the GNWT to obtain different financing terms, including advance payments and/or negotiate administration fees is very limited. In some cases the terms of the agreement may not be totally favourable and the financing and administration fees have to be absorbed by the GNWT otherwise these projects, which will benefit the residents of the Northwest Territories, will not proceed. As an example of these difficulties, in the area of health benefits, Health Canada has absolutely refused to provide advance payments and will only fund projects on receipt of proof of payment by the GNWT.

The GNWT is currently reviewing our policy in this area. This review is intended to address the three points raised by the Office of the Auditor General as well as some additional

issues we feel need to be addressed. As well, for the last several years, there has been more diligent follow up on the billing and collections of receivable related to these projects which has improved the GNWT's cash flow and reduced its financing charges.

Risk of errors in Formula Finance Grant

3.19 The Government of the Northwest Territories gets about 80 percent of its revenue from the federal government under this grant. For its budget and public accounts, the territorial Government needs to get the most accurate figure possible so that the annual surplus or deficit is shown reliably.

3.20 The potential for reporting errors is high. The calculation is complex and subject to different interpretations. Senior management should review the calculations in detail to verify their accuracy. In the past few years, we have reported orally and in writing to management on the need for improved reviews.

3.21 For the year ended 31 March 2002 and prior years, we noted during our audit a number of

significant adjustments were needed to correct the reported grant revenue. Management made the corrections.

3.22 Management has assured us that it now has appropriate review procedures to detect errors. These seem to be working, as we did not detect similar errors during our 2003 audit. We recognize the efforts of Government staff for making these improvements.

3.23 An incorrect Formula Finance Grant would distort the reported or forecasted financial condition of the Government. The GNWT needs an accurate calculation to ensure it receives all its revenues under the formula financing agreement on a timely basis. The territorial Government needs to have an accurate grant figure as there have been errors in the past and differing agreement interpretations.

3.24 The reduction in the number of errors detected in the Grant calculation as part of our 2003 audit indicates improvements have been made in the review process over the Grant. We continue to encourage the Government of the Northwest Territories to rigorously review the

grant calculation to ensure accurate presentation of revenues.

Department of Finance's response:

The Department agrees with the Auditor General of Canada that an accurate calculation of the Formula Financing Grant is critical for both budgeting and the public accounts.

The review procedures in place for the Grant calculation include:

- *reconciliation of NWT Finance calculations to Government of Canada's calculations.*
- *comparison of current year calculations to prior year.*
- *detailed analysis and follow-up on variances from estimates and prior years.*
- *a detailed review of the Grant calculation by someone other than the person who did the initial calculation.*

The review process resulted in no errors for the 2002-03 Grant calculation, with the exception of the change to revenue that affected the Grant calculation. The Department of Finance will continue to exercise all possible due diligence to ensure that the review procedures that it has set up will continue to be followed.

Revenue fluctuations—Corporate income taxes

3.25 The federal government assesses and collects income taxes on behalf of the GNWT. It uses a complicated method to separate the territorial Government's share, and then the federal government sends the money to the territorial Government. Because taxes can take several years to be finalized, the GNWT does not know exactly what its tax revenues are from year-to-year and has to use estimates that the federal government prepared, for budgeting and accounting purposes.

3.26 This means that the current method used to estimate the territorial Government's corporate income taxes is correct when calculated over several years. The territorial Government ultimately gets the correct amount of dollars in the long term. However, on an annual basis, this method can significantly distort the amount of funding received from Canada. The current method is set out in a formula that uses estimates from previous years' figures. The estimated corporate income tax also affects the Formula Finance Grant and the Canadian Health and Social Transfers (CHST) from year-to-year, making yearly

budgeting, accounting, and cash management difficult.

3.27 There are two examples of distortion in revenue that the territorial Government has to deal with. First, it receives funding that is higher than it should be, and that it will have to pay back in future years. Second, it receives funding that is lower than it should be, and that it will have to recoup in future years. Over the past few years, most initial payments of corporate taxes have been too high.

3.28 In normal years, corporate taxes are not large, given the small economy in the NWT. However, if a large one-time tax item occurs, complexities in the formula can distort annual funding for

several years to come, complicating the process of financial planning.

3.29 In both 1999 and 2000, private corporations, taking advantage of the low corporate tax rates in the NWT, declared large capital gains in the territory. This resulted in large windfall taxation revenues of more than \$400 million for the GNWT in those two years. These large amounts affected the corporate tax revenue stream for four years starting in 2000–2001.

3.30 The tax windfalls also impact amounts due under the Formula Finance Grant, plus the CHST for a number of years. Exhibit 3.2 shows the net impact of these two windfalls on the Government's annual revenue and bottom line.

Exhibit 3.2 Net impact on funding

<u>Fiscal year</u>	<u>Increase/(decrease) in Net funding (\$ millions)</u>
2000–2001	\$ 24
2001–2002	147
2002–2003	(40)
2003–2004*	<u>(15)</u>
Overall net increase	<u>\$ 116</u>

3.31 Because the estimates are based on previous years' tax figures, the net funding from the federal government was too high in early years. The territorial Government had to pay back millions to the federal government in the later years.

3.32 Although, the net \$116 million received over the four-year period is the actual net gain, the revenues reported annually in each of the four years were distorted, making budgeting and reporting more difficult and confusing.

3.33 The Government of the Northwest Territories should discuss with the federal government how to improve its estimates, meaning how to adjust for unusual items, in corporate income taxes for the NWT.

3.34 The Government of the Northwest Territories should review how it can make adjustments to estimates supplied by the federal government to ensure meaningful financial reporting.

Department of Finance's response:

Income tax collections for a year are not known with any certainty until

well after the end of the year, once most returns have been filed and assessed. Therefore, income tax revenue recorded for a year must be based on estimates of tax that will be collected for that year.

Finance Canada estimates the tax base for the country as a whole, based on macroeconomic data and forecasts, and allocates it among the thirteen provinces and territories. This procedure is included in tax collection agreements with the provinces and territories. While discussions have been held over how to improve the methodology, they have not yet resulted in significant improvements.

The Government of the Northwest Territories, as part of its forecasting, does estimate both Corporate and Personal Income tax for the previous year in March. While using the NWT estimates could, on average, lead to slightly better revenue being recorded, using the federal estimate provides a useful independent source for the estimates.

Chapter 4

LAND OWNERSHIP—TRANSFER FROM CANADA

Introduction

4.1 We have included this chapter primarily as an information update to highlight ongoing legal ownership issues for the Legislative Assembly.

Why is this important?

4.2 The transfer of land from the federal government to the Government of the Northwest Territories has been ongoing for decades, but is still not complete. This can cause complications, including costs and delays, when the Government (or one of its agencies) plans to develop or sell plots of land. Also, land claim settlements need resolution of issues of ownership of land before they can be completed.

Some background information

4.3 Commissioner's Land is land that has been transferred to the

Commissioner of the Northwest from the Government of Canada. When the land is transferred, the Commissioner has administrative control over the land and can sell, lease, or otherwise dispose of it, as set out in the *Commissioner's Land Act* and Regulations. However the land always remains vested in Her Majesty.

4.4 The Department of Municipal and Community Affairs (MACA) of the Government of the Northwest Territories is the custodian of Commissioner's Land and administers it in accordance with the *Commissioner's Land Act* and Regulations, on behalf of the Commissioner.

4.5 In 2001 and 2002, the Government of the Northwest Territories applied to have the land for nine airports transferred from the Government of Canada to the Commissioner, although the territorial Government had been responsible for and using these airports

for many years without the land having been transferred.

4.6 It is not always clear which land the territorial Government owns in the NWT and which the Government of Canada owns for the following reasons.

- In about half the communities the Government of Canada made a block transfer of ownership of all land to the Commissioner of the Northwest Territories
- In the other communities land usage and tenure were transferred without transferring ownership, establishing what are known as reserves
- All the land has not yet been surveyed. Land must be surveyed to transfer title

4.7 The Government of the Northwest Territories has had difficulties in the past when it has attempted to sell and transfer certain assets because of ownership issues. Ownership issues also need to be resolved for land claim settlements.

4.8 Over a three-decade period between 1970 and 2000, the federal government made block transfers of most of the land to the name of the

Commissioner in approximately half of the communities (see exhibit 4.1).

4.9 The block transfers did not pass all parcels of land to the Government of the Northwest Territories. For example, the federal government reserved specific lots for specific federal departments to use. These are known as federal reserves.

4.10 The federal government has not yet done a block transfer for the remaining communities. Much of the land in these communities is still in the name of Indian and Northern Affairs Canada (INAC), although some individual lots have been transferred to the territorial Government.

4.11 Land that is still in INAC's name but is used by the territorial Government are known as reserves as mentioned above. This is less time consuming and less costly than transferring individual land titles. However, if the GNWT wanted to sell that land, it would still need to have the land transferred to the name of the Commissioner.

4.12 Reserves are also established for GNWT departmental use on Commissioner's Land. The Department of Municipal and Community Affairs

(MACA) is the only department of the GNWT that can establish reserves on Commissioner's Land, or request the federal government to establish a reserve on Crown land on behalf of a GNWT department.

4.13 GNWT departments are not legally allowed to hold an interest in land. However, both the Northwest Territories Housing Corporation and the Northwest Territories Power Corporation are allowed to hold an interest in land.

4.14 Additional transfers from the federal government to territorial corporations in the past few decades have included houses owned by CMHC and transferred to the Housing Corporation and assets transferred to the Power Corporation, after the windup of Northern Canada Power Corporation. At the time, these transfers did not always include the transfer of the land.

Formal title transfers need to be done

Proper title needed to sell assets: Staff housing example

4.15 If MACA wants to grant title to a parcel of Commissioner's Land, but not to a GNWT department, it first needs to survey the land and then it can be

registered at the Land Titles Office and fee simple title can be given.

4.16 The territorial Government has legal problems when selling staff houses. The land titles offices in the municipalities blocked the sales. The offices couldn't register the title to the land as some staff houses were on land that had not been surveyed. These parcels of land can only be given a lot status and a land title after a formal survey, which can take up to a year.

4.17 Other staff houses were on land that had been surveyed, but with only a portion of the lot designated as the Commissioner's while other portions were still designated as federal land. This land cannot be sold because part of the land is still designated as federal land. The Government of the Northwest Territories can request the federal government to transfer this land, but this can take up to two years; this means that the sales cannot be made until then.

Land claim settlements

4.18 Land claim settlements need resolution of the ownership of land issues before they can be completed. The Dogrib Land Claim Settlement is an example.

4.19 The territorial Government has to identify clearly who owns land to be transferred as part of claim settlements. The Dogrib land claim settlement in 2003 required the territorial Department of Transportation to survey all land in the settlement region. This was a costly and lengthy process. MACA also conducted an extensive survey program in the Tlicho settlement area.

4.20 Resolving ownership issues can be expensive: The transfer from Northern Canada Power Corporation to the Northwest Territories Power Corporation is a good example.

4.21 The Power Corporation has spent significant amounts of money on land and title transfers since 1988, mostly getting formal surveys. The Power Corporation has now obtained easements, rights-of-way, or fee simple title for all significant sites, but continues to work on ownership. It plans an internal audit, which will look at outstanding Northern Canada Power Corporation transfers.

Current ownership issues

4.22 The Department of Municipal and Community Affairs (MACA) is verifying land ownership in all communities and expects to complete the work in about two years. MACA is working with other territorial departments to review and establish reserves for the lands that they are using. MACA has reserve listings for departments, which departments can use as a starting point to verify and update their interests.

4.23 On federal land where there is a reserve for a GNWT department, MACA hopes to seek an Order-In-Council from the federal government to have the land transferred to the Commissioner. MACA is also trying to identify all GNWT interests outside community boundaries.

4.24 The Government of the Northwest Territories should develop a government-wide plan, including agencies, to resolve all outstanding ownership issues, including proper surveys by a particular deadline.

Exhibit 4.1

Communities subject to block land transfer		
Aklavik	Deline (Fort Franklin)	Enterprise
Fort Good Hope	Fort McPherson	Tulita (Fort Norman)
Fort Providence	Fort Simpson	Fort Smith
Hay River	Holman	Inuvik
Norman Wells	Paulatuk	Pine Point
Rae Edzo	Sachs Harbour	Tsiigehtchic
Tuktoyaktuk	Yellowknife	
Communities not subject to block land transfer		
Colville Lake	Dettah	Ndilo
Fort Resolution	Jean Marie River	Kakisa
Lutsel K'e	Nahannii Butte	Rae Lakes
Trout Lake	Wekweti	Wha Ti
Wrigley		

Department of Municipal and Community Affairs' (MACA) response:

The Department is generally pleased with this chapter. MACA is please to advise that the Lands and Infrastructure Administration Division completed a strategic plan to guide the administration of Commissioner's Land, in late 2002. Four key strategies resulted from the plan, and include:

- ***Converting existing leases in settled land claim areas to fee simple title;***
- ***Transferring Commissioner's Land within municipal boundaries to community governing authorities;***
- ***Streamlining the process for the administration of federal land within municipal boundaries in cooperation with the Department of Indian Affairs and Northern Development; and***
- ***Improving existing land administration procedures.***

MACA is working towards developing programs and implementing solutions to satisfy the key strategies identified in the plan. With respect to resolving land ownership issues, MACA has been working on a Land Verification Project for the past two years. This

work involves identifying the ownership and legal status of each parcel of land within municipal boundaries, across the Northwest Territories. It is expected that this work will be completed in another two years.

Chapter 5

PROTECTING THE ENVIRONMENT - CLARIFYING RESPONSIBILITIES

5.1 The Northwest Territories faces significant challenges in protecting land, water, and air, for current and future generations. Not all of the responsibility belongs to the Government of the Northwest Territories; it requires the co-operation of many organizations and individuals. The territorial Government along with federal government, local governments, aboriginal groups, private industry, and residents of the Northwest Territory all have roles to play.

5.2 Here, we briefly highlight how the Government of the Northwest Territories works with the federal government on environmental issues. We will highlight different environmental issues in future reports to promote the consideration of the environment in the decisions of the Government.

5.3 The Government of the Northwest Territories and the federal government both have legislated responsibilities for the NWT environment. Because neither of these levels of

government have unlimited resources, they have an incentive to minimize duplication and avoid jurisdictional disputes. The two governments also need to work together to ensure that there are no gaps in environmental standards.

5.4 The Government of the Northwest Territories and the Government of Canada try to avoid duplicating each other's efforts. The federal government does some things for the territorial Government and vice versa. For example, in the 1985 Spills Working Agreement (updated in 1999) between the governments, they agreed that whoever is in the best position to respond to a spill will take action. If the federal government does not have staff in a particular region where a spill occurs (on federal property or land), the GNWT will respond and will turn over the investigation when the federal representatives are available. This type of working arrangement is a practical approach to deal with territorial and federal environmental legislation and limited capacities.

5.5 Although both levels of government have an incentive to work together to avoid disputes, disputes can occur.

5.6 Sometimes, responsibility for an environmental liability can be unclear, which can lead to disputes. The Giant Mine case is an example. When the Giant Mine began in 1948, the land was administered by the federal government. The mine operated under federal administration for 22 years.

The Giant Mine has three types of environmental liabilities:

- underground: the federal government has assumed full responsibility for this because of its jurisdiction over minerals.
- water-related liabilities: the federal government has full responsibility because of licensing under the federal Waters Act and more recently, the Mackenzie Valley Resource Management Act (MVRMA).
- non-water, surface liabilities: the staff of the Government of the Northwest Territories informed us that the federal government believes the liability should be shared with the GNWT as land administration was transferred in 1970. This made the

territorial Government responsible for pollution that occurred subsequent to that. The GNWT's view is that the federal government has responsibility for the liability because the mine exists through federal authorizations.

5.7 The Government of the Northwest Territories should reach agreements with the Government of Canada where responsibility for environmental liabilities is not clear between these two governments.

5.8 Finally, the Government of the Northwest Territories, the Government of Canada and Aboriginal boards established under the MVRMA are working to improve the efficiency of the existing environmental assessment and regulatory processes in light of the proposed pipeline down the Mackenzie Valley and other non-renewable resource developments.

Related information

5.9 The 2002 Report of the Commissioner of the Environment and Sustainable, Chapter 3, refers to abandoned mines in northern Canada as complex, contaminated sites, inherited by the federal government from past private-sector mining operations. The Report

noted that these sites pose serious health and environmental threats and examined how Indian and Northern Affairs Canada managed them. The Report also looked at the measures taken to ensure that such mining companies pay for the cleanup of environmental problems they create now and in the future. The full report is available on the Web site of the Office of the Auditor General of Canada, www.oag-bvg.gc.ca.

Department of Resources, Wildlife and Economic Development's response:

The GNWT agrees that the federal and territorial governments need to continue working towards reaching an agreement where responsibility

for environmental liabilities is not clear.

With respect to the future management of contaminated or hazardous waste sites on federal Crown Land, this matter is the subject of on-going discussions through the Northwest Territories Land and Resources Devolution negotiations.

With specific reference to the Giant Mine, the GNWT invited the Department of Indian Affairs and Northern Development to enter into discussions aimed at reaching an agreement on the remediation of surface liabilities at the mine site in November 2001. These negotiations are continuing with no agreement having yet been achieved.

Chapter 6

OTHER

Division of the Northwest Territories Power Corporation

This chapter contains items for the information of members of the Legislative Assembly.

6.1 When the governments of the Northwest Territories and Nunavut agreed to split the Power Corporation, they set a target for completion of 1 November 2001. As at March 2003, the division was incomplete with several millions of dollars still in dispute.

6.2 A root cause of the problem is a poorly worded division agreement. This allowed conflicting interpretations by government representatives from Nunavut and the Northwest Territories. It was a key cause of the delays and used valuable resources on both sides. The conflicting interpretations put an unnecessary strain on the relationships between the Northwest Territories Power Corporation and the Nunavut Power Corporation, and between the governments.

6.3 The agreement lacks clarity and detail in certain areas. For example, it does not provide clear details on how operations continuing after 1 April 2001 should be divided. This lack of detail has led to lengthy negotiations and resources being used to support each side's position.

6.4 The conflict resolution guidance in the agreement is not clear, which has also contributed to delays. The agreement does not set time limits for adopting resolution guidelines and offers different conflict resolution options that the two territorial governments cannot agree upon.

6.5 A lesson can be learned from this experience when drafting future agreements.

6.6 In negotiating agreements, the Government of the Northwest Territories should ensure that clauses are written with sufficient detail and clarity to minimize the possibilities

that the parties will be able to interpret them differently.

6.7 When the Government of the Northwest Territories is involved in negotiating agreements, it should also make sure that the actions to be completed contain specific time-bound mechanisms to resolve differences efficiently.

Government's response:

The OAG has expressed an opinion that the clauses in the "Division of the NTPC Agreement" lacked sufficient clarity and detail making it possible for the parties to interpret them differently and that actions should contain specific time bound mechanisms. It is the position of the GNWT that:

The fact that an interpretational disagreement has arisen between the Government of the NWT and the Government of Nunavut does not mean the agreement is unclear. The GNWT believes the agreement is very clear and that the GN's interpretation is without merit. No agreement can be so carefully

crafted as to prevent one party from choosing to challenge its intent which is why contract interpretation is one of the most prevalent matters before the courts. The GNWT shares the concern over the length of time it has taken to resolve this issue, although is unsure that time limited dispute resolution provisions would have over-ridden the capacity issues that the Government of Nunavut faced at its creation and continues to have to deal with today.

Services and facilities provided without charge to government agencies

What is the issue?

6.8 The Government of the Northwest Territories and its various corporations and other agencies provide a range of services to GNWT residents, including housing, power, and social and health payments. Because of the way the territorial Government is organized, in many cases the costs of providing the services are not specifically identified, while the cost of other services are recorded in other departments or programs.

6.9 Legislators should be given sufficient information on all programs to be able to decide if the program is effective and at what cost. This section of the chapter deals only with the cost aspect.

6.10 We are concerned that the costs of several important programs have not been identified correctly due to cross subsidization that is subsidizing a corporation by paying some of its expenses, and unidentified costs. This makes it difficult to decide if a program should be continued, expanded, or cut back. Without knowing the full costs, one cannot know if programs are economical or efficient.

6.11 An important piece of information for some programs, especially for Crown corporations, is their financial statements. If these contain all the pertinent information on costs and revenues, legislators can use them, along with program performance information, to review and assess program success, and to determine whether changes are needed.

6.12 However, some activities in corporations do not fully identify all their costs. Examples include Aurora College, the Petroleum Products

Revolving Fund, the Northwest Business Credit Corporation and the Northwest Territories Liquor Commission. This is because the territorial Government provides services and facilities to them without charge, and the corporations' financial statements do not reflect their full costs of operations.

6.13 For example, full costing information is needed before the legislators can know how much it costs to educate a student at Aurora College. How much does it cost the territorial Government to be a lender of last resort through the Business Credit Corporation?

6.14 In some cases there are no formal agreements between the Government and its agencies for the provision of services and facilities. The responsibilities of both parties may not be clear.

Aurora College and the Petroleum Products Revolving Fund use government facilities at no charge

6.15 The Government built campuses and student housing for Aurora College over the years. These assets are not carried on the College's books, nor are the costs of financing them. The Petroleum Products Revolving Fund (the

Revolving Fund) uses tank farms owned by the Government, and although the costs are shown in a financial statement note, they are not booked to the Revolving Fund. Nor does it show the financing costs of buying and stocking fuel, which are also paid by the Government.

6.16 Aurora College uses two campuses, certain student housing units, and community learning centres owned by the Government, through the Department of Education, Culture and Employment without rental charges. There are no written agreements between the College and the Department for these facilities.

6.17 In its financial statements of 30 June 2003, the College added note disclosure on the Government's amortization expense for the buildings as a proxy of what the College's costs could be. This is a move in the right direction, but the College's statement of operations still do not reflect these costs.

6.18 Figures from the College's annual reports showed that an average cost per full-time-equivalent student was \$27,475 for 2002, and \$25,446 for 2001.

These averages do not include the costs of using the Government-owned facilities or other services received without charge.

6.19 If the amortization and financing costs of these facilities, plus other uncharged services were included, the total costs of the College would have been about \$1 million higher, or about \$800 more per student.

6.20 Because there is no written agreement, the responsibilities of both parties, the College and the Government, regarding the use of these facilities are not documented. Implicitly, the College's tenure of these facilities is for an indefinite period, but it has never been formally contracted. The College operates and maintains the buildings, receiving annual funding from the Department of Education, Culture, and Employment. The College uses the Department of Public Works for operating and maintenance services, and the Department of Finance is responsible for risk management (that is, ensuring adequate insurance) for the facilities. A formal agreement would ensure the roles and responsibilities of both of the entities involved in each of these service arrangements are clear and documented.

6.21 The Government of the Northwest Territories should ensure that when one agency uses another agency's assets or services, an agreement outlining each party's responsibilities is prepared.

Other services provided without charge

6.22 The Government also provides other services without charge to the College, including payroll processing, insurance and risk management, legal counsel, construction management, records storage, computer operations, asset disposal, project management, and translation services.

6.23 The Government provides similar services, without charge, to the NWT Business Credit Corporation, including accounting support, regional and human resource services, office accommodation, and some capital assets.

6.24 These costs are not recorded in the financial statements of the two entities, although they are noted. A financial statement note is better than no estimate at all but is not as good as recording the actual cost in the statement of operations.

6.25 For the facilities and other services presently provided without charge, the Government of the Northwest Territories should improve accountability by recording them in the appropriate entity's financial statements.

Financial Management Board's response:

The Financial Management Board (FMB) is aware of the services provided without charge to government agencies and the associated cost and benefits of this arrangement. The value of the services, with the exception of the use of tangible capital assets, has been disclosed in the notes to the financial statements of the affected agencies. The 2004 Petroleum Products Revolving Fund statement of operations includes all services provided without charge with an offsetting contribution from the GNWT. This method fully discloses the Government's subsidy to this program. The FMBS will undertake to review current policy with a view to improving disclosure of services provided to all government agencies without charge.

Consolidated budget

6.26 At present, the Government's budget and financial statements are not comparable. This makes the budget data less than fully useful when comparing the budget to later financial statements showing revenues and spending. This is because they are prepared, using different methods. The Government's budget is not consolidated, whereas the financial statements are consolidated.

What does this mean?

6.27 The budget shows departmental spending, including contributions, made to territorial corporations. The budgeted revenues and spending of the corporations themselves are in separate budgets. The financial statements include details of the corporations' revenues and spending, except for the Workers' Compensation Board, which is not consolidated at all, and the Power Corporation where the consolidation is not on a line-by-line basis and includes only the Government's equity. This is because the Power Corporation is financially self-sufficient and does not get government funding.

6.28 The Government of the Northwest Territories has adopted as its accounting standard the recommendations of the Public Sector Accounting Board (PSAB). These require, among other things, that the Government prepare consolidated financial statements, which it does.

6.29 The rules do not require the Government to prepare a consolidated budget. Yet this could be useful to both managers and members of the Legislative Assembly, if they wish to compare consolidated financial results with what was budgeted.

6.30 The Government's financial statements are consolidated by adding together like items of assets, liabilities, revenues, expenses from the financial statements of the Government and the corporations that are a part of the "reporting entity" which include:

- government departments and revolving funds,
- the Northwest Territories Housing Corporation,
- the Northwest Territories Business Credit Corporation,
- the Northwest Territories Development Corporation, and
- Aurora College (the College).

6.31 Where the corporations do business with each other and with the Government, the transactions are taken out of the consolidated financial statements to avoid inflating Government revenues and expenses.

6.32 A consolidated budget would also help focus more attention on the broader activities of the Government. This is not possible now. A consolidated budget would also show such things as how much is spent on salaries and administration. This could assist in evaluating overall Government efficiency in delivering services.

6.33 Supplementary information in a consolidated budget could continue to give members information on how money is being spent on various activities such as housing and post-secondary education. Under the current system, members of the Legislative Assembly approve contributions to the Housing Corporation, the College, the Business Credit Corporation, and the Development Corporation. The Main Estimates also detail their activities ranging from a detailed breakdown of activities and costs for the Housing Corporation, a summary breakdown of activities and costs for the College, and

brief descriptions of the Business Credit Corporation and DevCorp activities.

Recent changes to guidance from the Public Sector Accounting Board

6.34 The Public Sector Accounting Board recently made changes to what the Government's reporting entity should include. Under these new provisions the Government reporting entity should include entities that are controlled by the Government. Control is defined for purposes of these new changes as the power to govern the financial and operating policies of another organization with expected benefits or the risk of loss to the government from the other organization's activities.

6.35 These changes will be applied for fiscal years beginning on or after 1 April, 2005. The impact of these changes could be significant. These changes might result in the GNWT having to include health and education boards in its consolidated financial statements. If this happens, the existing differences between the budget and the financial statements would be even greater. The impact of these changes on the financial statements needs to be assessed in the context of the Government's budgetary process.

Government's response:

The GNWT has expressed to PSAB its opposition to consolidating all boards and agencies in government budget documents and financial statements including producing consolidated budget figures. The administrative effort involved, and the additional intrusion into board operations, negates any theoretical value of further consolidation. In fact, we question whether financial statement value would be enhanced

as it is our view that further consolidation of the nature suggested would increase the complexity of our statements, require significantly more user sophistication, and actually detract from the clarity and accuracy of the financial information presented. These types of changes would soon bring us to the point where financial statements were only understandable by trained accountants with significant amounts of time to invest in scrutinizing and understanding them.

Appendix I

Our People

Many people with different skills and experiences carry out an audit. It is the sum of these resources that allows the Office to make a difference. The team responsible for the audit of the GNWT includes:

Auditor General Sheila Fraser, FCA	
Assistant Auditor General Ronald C. Thompson, CA	
Principal Roger Simpson, FCA	
Audit Staff	
Amy Begley	Susan Meilleur
Chantal Berger	Marjorie Pound
Barbara Britt	Julie Paille
Kristine Coombes	Megan Picard
Darlene Holloway	Chris Polselli
Dustin Hoshowski	Donna-Lee Shaw
Mary-Jo Jacksic	Mila Simon
Stephanie King	Dan Stadlwieser
Tyleen Kearney	Peter Yeh
	Randy Zamrykut
Other Audit Services	
Annual Audit Practice Team Edit and Graphics Services Legal Services	