



**Report of the Auditor General
of Canada to the Legislative
Assembly of Nunavut—2005**



**Office of the Auditor General of Canada
Bureau du vérificateur général du Canada**

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Report of the Auditor General of Canada to the Legislative Assembly of Nunavut—2005

Auditor General's preface

This is my fourth report to your Legislative Assembly.

On 1 April 1999 Nunavummiut were filled with optimism at the creation of a new territory and government. They were justifiably proud of the smooth transition from the Government of the Northwest Territories.

I submitted my first report to the Legislative Assembly of Nunavut in 2001. Since then I have repeatedly emphasized the importance of good financial management and the need for improvement in this area by your government. In this report I want to take stock of the past and present situation in Nunavut, and offer recommendations for improvement.

The importance of financial management. Good financial management reduces the risk of mistakes, bad decisions, or fraud. Basic financial controls are essential for good government. Because the Government of Nunavut does not yet have basic financial controls in place, the risk of problems is greater than it should be.

Current financial management is weak and fragile. To have basic financial controls in place, any organization needs to give attention to six broad areas. Six years after Nunavut's creation, I am surprised at how slowly financial management has improved. The government needs to do more in each of the six areas.

Financial management is certainly stronger now than when Nunavut was created. However, overall your current financial management is weak and fragile. It has not adequately reduced the risk of error, bad decisions, or fraud. In some cases, when one qualified person leaves, a part of the government's finance functions comes close to shutting down until a replacement is found, sometimes months later.

Examples of problems. Chapters 1 through 5 of my report provide examples of weaknesses in Nunavut's financial management.

There is no doubt that the members of your public service take their responsibility seriously, and are trying to improve financial

management. However, so far their efforts are not translating into sustainable, long-term improvements.

Structural problems. Why are these efforts unsuccessful? Chapters 6 and 7 of my report discuss structural problems within the government that are barriers to improving financial management.

Chapter 6 focusses on your government's computer systems. The Government of Nunavut is a billion-dollar-a-year operation, yet many of its key financial systems still rely on manual systems, or systems developed using generic spreadsheets that lack the controls found in regular systems. These systems are therefore prone to error.

Chapter 7 examines your government's structures. Your accounting staff is spread throughout Nunavut in small, decentralized groups. Large organizations need professional accountants to provide financial leadership. At present your government does not have enough professional accountants for such a decentralized environment, and certainly not enough to deal with all the problems needing attention.

Solutions. Chapter 8 of this report looks at options to give financial management the rapid boost it needs. Your government could continue to try small changes, as it has done for the past six years. However, this approach has not worked so far and there is no reason to believe that it will work in the future.

Your government could hire more professional accountants with the expertise needed to deal with problems. However, hiring is difficult as well as expensive, and out-of-territory recruitment would increase competition for staff housing.

In Chapter 8, I recommend some degree of recentralization to establish basic financial controls in your government. That is, some accounting functions need to move back into larger groups. Eventually, when there have been significant improvements in financial management, the government could again consider decentralizing certain accounting functions.

Chapter 8 goes on to examine recentralization in relation to the government's decentralization policy, training for Nunavut Land Claims Agreement beneficiaries, and services to the public. It concludes that recentralization need not conflict with these priorities.

Three key recommendations. Throughout my report I make recommendations for dealing with issues I observed during my audits. Most of these concern specific problems.

However, I want to highlight three of the more fundamental recommendations here.

- Paragraph 131 in Chapter 6 recommends that the government review its accounting systems and deal with gaps in formal systems that block improvements to financial management. For example, the government does not have main accounting systems for loans or inventory.
- Paragraph 160 in Chapter 8 recommends that the government review its accounting structures (including the physical location of staff) and, to some degree, recentralize accounting functions to deal with the root causes of problems that block improvements to financial management.
- Paragraph 180 in Chapter 8 recommends that the government launch a new program to produce Land Claims Agreement beneficiaries who are professional accountants, on the model of its successful program to produce beneficiaries who are lawyers. The program will prepare beneficiaries for senior positions in financial management.

Ultimately, good financial management is part of the foundation of good government. I recommend your government take steps now to implement the controls it needs in order to provide high-quality services to all Nunavummiut for years to come.

Chapter 1

The government needs to improve its financial management in many areas

Good financial management is essential for good government

1. Mistakes happen. Bad decisions happen. Fraud can happen. But the risk of such problems is lower in an organization with good financial management, and good systems and practices.
2. Our previous reports to the Legislative Assembly have all dealt with the importance of good financial management. Among other information, the reports present a five-step model for assessing financial management and guiding improvements. The reports are posted on our Web site at www.oag-bvg.gc.ca.

Past efforts to improve financial management

3. Six years have passed since the creation of the Territory and Government of Nunavut. Our reports to the Legislative Assembly have all focussed on the need for the government to move beyond the start-up phase and achieve mature financial management.
4. The government has made a number of efforts to strengthen financial management. For example, it has conducted evaluations, created a Crown Agency Council to focus on Crown corporations, and held two conferences on financial management.
5. In response to recommendations in our 2001 report to the Legislative Assembly, the government committed to putting in place basic financial controls by 2004. Our 2004 report noted that the government had not met this commitment.

Does the government have basic financial controls yet?

6. **Our assessment of controls in 2003–04.** There are six broad areas in which a government needs to have proper financial controls: transactions, data, reporting, comparing plans and results, generating revenue, and monitoring.
7. The government's financial management is certainly better today than when Nunavut was created. Nonetheless, during our 2003–04 audit work we observed serious deficiencies in all six control areas. These indicate that the government does not yet have basic financial controls (Exhibit 1.1).

Exhibit 1.1 Examples of financial management problems in the Government of Nunavut, 2003–04

Control area	Problem(s) observed
Controls over financial transactions	In about ten percent of the payment vouchers we reviewed, signing authorities were not followed (paragraph 11).
Controls over quality of financial data	We found errors in about 50 percent of leave records we reviewed (paragraph 13).
Ability to report in accordance with statutory requirements	The government missed the deadline for tabling its 2003–04 consolidated financial statements by about a year. MLAs and others do not have timely financial information (paragraph 18).
Ability to prepare plans and budgets, and to report against them	Main estimates cannot be directly compared to audited, consolidated financial statements. Financial statement readers cannot compare budgets to actual results (paragraph 21).
Ability to generate necessary revenue	The government is slow to collect money due to it under cost-sharing agreements (paragraph 22).
Monitoring and controlling operations	We found numerous cases of non-compliance with Nunavut's financial laws, including seeking the Legislative Assembly's approval to spend money after it had already been spent (paragraph 28).

8. Government's own assessment of controls in 2004–05.

As part of its efforts to improve financial management, the government has formally assessed the state of its controls from time to time. In late 2004–05, a government report concluded that essential controls were not yet in place.

9. While our 2004–05 audit work continues, we have already seen enough problems to agree with the government's own assessment that significant problems remain.

A closer look at financial management problems

10. This section looks more closely at the financial management problems noted in Exhibit 1.1. These are only some of the problems we found during our audit work.

11. Signing authorities not followed: past problems continue.

In our previous reports to the Legislative Assembly we noted that payments were being made without proper approvals. In our 2003–04

audit work we found the same problems. Around ten percent of payment vouchers we reviewed lacked proper approvals, for either the vouchers themselves or supporting documents. The problems should have been caught before payment was issued. The practice of making payments without proper approvals greatly increases the risk of error or fraud.

12. Chapter 2 discusses this issue in detail and provides our recommendations.

13. **Errors in manual leave records: past problems continue.** In previous reports and still in our 2003–04 audit work we noted frequent errors in individuals' manual records for leave, such as annual vacation and sick leave. Around 50 percent of leave records we examined in our 2003–04 work had some sort of error in leave balances. Sometimes leave balances were too high based on supporting documents, and sometimes too low.

14. The use of manual leave records worsens this problem. It is unusual for an organization with 2,300 employees to still use manual records for leave.

15. Chapter 6 discusses the need to move away from manual or informal accounting systems for a number of areas, including leave records. Government officials have informed us that a new personnel system, now in development, will support computerized leave records.

16. Until computerized leave records are in use, the government needs to take steps to reduce the error rate of its manual records. During our work we observed that simple mechanical errors cause most of the problems. For example, the amount of leave on an application for leave form may be incorrectly entered on leave records, or there are errors in totalling leave records. In our view, training can help solve such issues.

17. **Recommendation.** While manual leave records remain in use, the government should continue training to reduce errors.

Government response. The government agrees. Additional training will be provided as required.

18. **Late financial statements: past problems continue, situation worsening.** The federal *Nunavut Act* requires the territorial government to table its consolidated financial statements no later than 31 December for the preceding fiscal year. The government has never met this deadline. Until recently it tabled the statements in May or June, five or six months after the statutory deadline.

19. For 2003–04 the situation is even worse. The government did not table its 2003–04 audited, consolidated financial statements until 16 December 2005, 20 months after the end of the fiscal year.

20. Chapter 4 discusses the reasons behind the late tabling and offers recommendations.

21. **Main estimates cannot be directly compared to audited, consolidated financial statements: past problems continue.** In our past reports we noted that the basis of accounting used for financial plans set out in the main estimates differs from that used in the government's consolidated financial statements. Consequently, readers lack a fundamental analytical tool: they cannot compare budgets to actual financial results. Chapter 5 discusses this problem further and provides a recommendation.

22. **Delays in collecting money due to the government under cost-sharing agreements: some improvements but government-wide effort required.** One element of good financial management is collecting money as soon as possible in order to generate cash. Our previous reports have noted billing and collection problems in various parts of the government.

23. The problems typically involve agreements under which the Government of Canada will reimburse the Government of Nunavut if it demonstrates that it has spent a required amount of money on a certain program. On 31 March 2004 we noted that Nunavut had an average of over six months of receivables under several such agreements.

24. While our 2004–05 audit work is not yet completed, it shows that the government has made significant progress in collecting receivables for two of the larger agreements.

25. Cost-sharing agreements are a major source of revenue for Nunavut. It is important to collect cash under them as soon as possible in order to pay for the government's expenses. This is a complex process, however: Nunavut needs to prepare claims and then satisfy Canada that the claimed amount is appropriate.

26. At present, several Nunavut departments have responsibility for billing and collecting money under individual cost-sharing agreements. Amounts outstanding remain significant. A government-wide review of the agreements could identify further opportunities for faster billing and collection.

27. Recommendation. The government's Internal Audit Services Branch should review all major cost-sharing agreements to identify opportunities for faster billing and collection.

Government response. *The government agrees. The Department of Finance will be working closely with other Government of Nunavut departments to ensure that they disclose all major cost-sharing agreements, and identify opportunities for faster billing and collection. In addition, there will be quarterly reporting of cost-sharing agreements to improve disclosure and collection.*

28. Non-compliance with Nunavut's financial laws: past problems continue. The Government of Nunavut has a responsibility to operate in accordance with the laws of Canada and Nunavut. Chapters 2 through 4 give numerous examples of the government's failure to comply with laws. The chapters also present our recommendations.

Chapter 2

The government has not consistently operated in accordance with the wishes of the Legislative Assembly

29. Chapters 2 through 4 of our report discuss aspects of the need for the government to operate in accordance with laws. This chapter outlines general principles and cites instances in which the government has not operated in accordance with laws.

30. Legislatures pass laws specifying how a government is to operate, and government officials must act in accordance with those laws. For example, a government cannot collect taxes or spend money without the legislature's approval.

31. Managers need to be aware of the direction given by the legislature and to act in accordance with it.

32. **Nunavut's financial authorities are complex.** The Government of Nunavut must comply with both federal and territorial laws (Exhibit 2.1). It must also comply with regulations and other rules.

Exhibit 2.1 Examples of laws (authorities) that specify how the Government of Nunavut should manage its finances

<i>Nunavut Act</i> (Canada)	This federal act sets out general requirements for spending money, the deadline for tabling Nunavut's financial statements, and the form they must follow. It also establishes a debt cap.
<i>Financial Administration Act</i> (Nunavut)	This legislation sets out detailed rules on spending and collecting money, financial statements, and financial management for all parts of the territorial government—departments, revolving funds, and Crown corporations.
Other acts	Many other acts set out financial rules: <ul style="list-style-type: none">• Appropriation acts authorize government spending.• Tax acts authorize taxation types and rates.• Loan acts authorize the government to make loans to third parties.• Enabling acts set rules for individual Crown corporations.

33. These laws are both lengthy and complex. For example, the *Financial Administration Act* alone contains over 50 pages of detailed rules that the government must follow. Government employees must understand these authorities as required by the position they hold (Exhibit 2.2).

Exhibit 2.2 Depending on the requirements of the position they hold, government employees need to understand financial authorities (laws, regulations, and other rules)

- Anyone who receives money or approves payments needs a basic understanding of his or her responsibilities.
 - To carry out their jobs properly, people who handle day-to-day processing of financial transactions need a greater appreciation of financial rules.
 - To ensure that special situations are handled properly, more senior staff who supervise accounting operations need a comprehensive understanding of the *Financial Administration Act* and other laws applicable to their areas.
-

Reservations in audit reports

34. Our audit reports indicate whether, in our opinion, the government has complied with key financial authorities.

35. Exhibit A.1 in Appendix A lists “reservations”—cases in which we have noted non-compliance with key authorities, or significant problems with financial statements. Exhibit 2.3 discusses these reservations.

36. Reservations in our audit reports are not common. They indicate significant problems. They signal issues that we regard as critical, requiring the government’s attention.

Signing authorities

37. Signing authorities specify which people in an organization may approve financial transactions and what kind of transactions they may approve. Our past audits found inconsistencies in the way staff enforced signing authorities. The problems persisted in 2003–04: around ten percent of payments we examined did not have proper approval.

38. This situation raises two concerns. First, it suggests that people processing transactions do not have a good understanding of the rules in place. Second, with this level of non-compliance, the risk of error or fraud is higher. The government needs to take steps to solve the problem.

39. In our view, one part of the solution is ongoing training in all aspects of authorities. The other part is increased monitoring and enforcement. The government's Internal Audit Services Branch now routinely audits signing authorities. Since violations persist, internal audit of signing authorities needs to continue.

40. Recommendation. To ensure that employees with financial responsibilities can do their jobs, the government should continue training them to be aware of all necessary authorities.

Government response. The government agrees. It will continue to hold information sessions on key Financial Administration Manual directives.

41. Recommendation. To monitor progress in reducing payments made without proper approval, the government should continue internal audit work on signing authorities.

Government response. The government agrees. The work of the Internal Audit Services Branch will continue, including audits and training sessions.

Exhibit 2.3 Reservations about the enforcement of financial authorities

Following are reservations in audit reports made public since our last report to the Legislative Assembly.	
Government of Nunavut	<p>Over-expenditures. Our opinions on the government's 2002–03 and 2003–04 financial statements contain reservations concerning departments that spent more money than approved by the Legislative Assembly. Chapter 3 of this report discusses the issue in detail.</p> <p>Late audited, consolidated financial statements. We have noted our concerns about missed tabling deadlines in all our previous reports to the Legislative Assembly. Given the lack of progress in this area, our 2003–04 opinion adds a second reservation about the late tabling of audited, consolidated financial statements. Chapter 4 discusses the issue in detail.</p>
Qulliq Energy Corporation	<p>Borrowings higher than allowed. The <i>Qulliq Energy Corporation Act</i> limits borrowings of this Crown corporation to three times its equity. Our opinion on the 2003–04 financial statements includes a reservation to highlight the fact that borrowings are \$4.7 million higher than allowed under the Act.</p> <p>Our 2004–05 audit report is without reservation.</p>
Nunavut Business Credit Corporation	<p>Various issues. Our 2002–03 and 2003–04 audit reports both contain reservations:</p>
2002–03	<ul style="list-style-type: none"> • For one new loan and one write-off of an existing loan, documentation of the Board of Directors' approval was not available at the time of our audit. • The Corporation continued to play an active role in the management of an outside organization, beyond the date set by the government for ending this involvement. • The Corporation was significantly late in submitting its annual report to the minister responsible for its operations.
2003–04	<ul style="list-style-type: none"> • For one new loan, the Board of Directors' approval was not available at the time of our audit.

The debt cap

42. The Government of Canada has set a limit on the amount of debt that the territorial government can incur (Exhibit 2.1). The limit is currently \$200 million.

43. We explored the importance and complexity of the debt cap in our previous reports to the Legislative Assembly. The government needs to have a sense of the amount of its actual borrowings to ensure that it does not inadvertently approach or exceed the debt cap. Some points must be borne in mind, however:

- Debts of all parts of the government need to be considered, not just of departments.
- Items such as bank overdrafts might also be considered debt for purposes of the debt cap. Calculation of debt for purposes of the debt cap is therefore complex.
- It can take months for the government to determine where its finances stand at the end of a fiscal year (Chapter 4). However, it should monitor debt and its relationship to the debt cap throughout the year.

44. In our 2004 report to the Legislative Assembly we recommended that Nunavut report where its actual debt stands against the debt cap in its audited, consolidated financial statements. This is a best practice of the Government of the Northwest Territories.

45. In response to a related recommendation by the Assembly's Standing Committee on Government Operations and Accountability, the government committed to doing this for the 2004–05 fiscal year.

46. Because of the complexity of determining debt for purposes of the debt cap, our Office has offered to work with the government to develop a common understanding of what is and what is not debt for purposes of the debt cap.

47. **Recommendation.** The government should disclose debt for purposes of the debt cap in its 2004–05 audited, consolidated financial statements.

Government response. The government agrees. This information will be included in the 2004–05 audited financial statements.

48. Beyond disclosing debt at year-end, the government needs to comply with the debt cap at all times. In our view, at present there is a risk that the government could reach the debt cap and not even realize it until much later. The risk exists because the government generally

considers only cash receipts and payments throughout the year (paragraph 61). In addition, the government takes into account the financial position of Crown corporations only at year-end.

49. The degree of risk depends on several factors, including how close the government is to the cap, the government's cash position, and the likelihood of bad financial news from Crown corporations. The risk is not zero, and prudence suggests developing procedures to guard against inadvertently hitting the cap.

50. Recommendation. The government should develop procedures for monitoring the debt cap throughout the year.

***Government response.** The government agrees. A Treasury function is being established in the Department of Finance, and will be operational for the 2006–07 fiscal year. Part of this function will be to monitor and report the Government of Nunavut's debt on a quarterly basis.*

Chapter 3

The government has a history of spending money without approval

51. It is a fundamental principle of our parliamentary system that a government should not spend money until its legislature approves the expenditure. The *Financial Administration Act* enshrines this principle, and sets out specific requirements for the Government of Nunavut. The government breaks the law when it spends money before receiving approval from the Legislative Assembly.

52. Rules in the *Financial Administration Act*. Two main principles in the Act guide spending by departments (Exhibit 3.1). While it is possible to obtain approval after money is spent, managers ought not to overspend in the first place.

Exhibit 3.1 Two main principles for spending by departments

- In its total operations and maintenance budget or its total capital budget, a department cannot spend more money than has been approved by the Legislative Assembly. Approvals for spending normally come from main estimates, or supplementary estimates approved either before the fiscal year or in the same fiscal year as the spending.
- If a department spends more than approved, the government must submit a supplementary appropriation to the Legislative Assembly in a later fiscal year. This highlights the overspending and requests the Assembly's approval for the spending after the fact.

In addition, there are special provisions to deal with emergencies and situations that occur when the Legislative Assembly is not sitting.

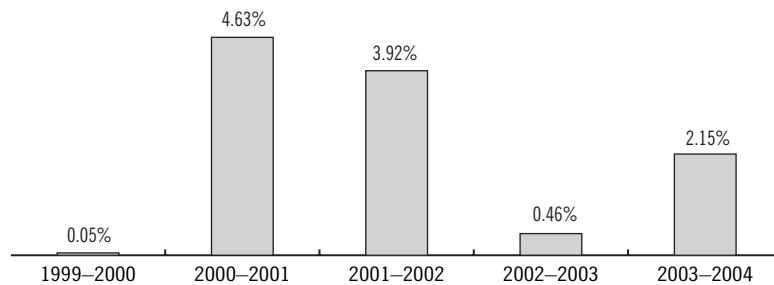
A history of breaking the rules

53. In every year since Nunavut's creation for which the government has tabled its audited, consolidated financial statements (1999–2000 through 2003–04), the government has violated the *Financial Administration Act* by spending money before it received approval from the Legislative Assembly. Government officials indicate that no such violation occurred in 2004–05. However, as of late November 2005 the government has not completed its consolidated financial statements for 2004–05, and we have not completed our audit of that year.

54. The amount of reported overspending varies depending on whether financial statements take account of supplementary appropriations. To determine the size of the problem, the best measure

is the total amount of spending for which the government sought approval from the Assembly after year-end. Exhibit 3.2 presents the percentage of total spending in each fiscal year for which the government sought approval from the Assembly after the fact.

Exhibit 3.2 Percentage of total spending approved after year-end, by fiscal year



Underlying causes

55. There appears to be no one reason for this problem. In some cases appropriations were exceeded because accounts payable were recorded at year-end.

A serious issue requiring immediate attention

- 56.** To stay within budget, managers need to
- have adequate information
 - give attention to detail
 - understand their department's operations in order to estimate future expenses accurately
 - be committed to not spend money without the Assembly's approval

It is simply not normal for governments in Canada to overspend. Other governments usually manage to live within budgets set by their legislatures. Nunavut's failure to do this is another indication that the government urgently needs to improve its financial management.

57. Recommendation. The Government of Nunavut should take immediate steps to ensure that it asks the Legislative Assembly for approval of spending in advance rather than after the fact.

Government response. *The government agrees. It has implemented procedures to ensure that departmental appropriations are sufficient to fund expenditures and that approval is sought prior to actual spending of public funds. These procedures include enhancement of the budget variance report process and strengthening person-year controls. The government will continue to strengthen financial controls in this area.*

Chapter 4

The government has not provided timely financial information to the Legislative Assembly

58. This chapter discusses the government's inability to provide the Legislative Assembly with timely financial information required by law.

59. The chapter also provides our overall conclusions on the government's difficulty in operating in accordance with authorities.

The importance of timely financial information

60. The government needs to table required financial information as soon as possible for three reasons:

- Various laws set deadlines for tabling information.
- Members of the Legislative Assembly (MLAs) and others need timely information to assess Nunavut's finances.
- More timely financial statements would also help managers by providing them with better information throughout the year.

This third reason requires explanation.

Lower-quality financial information throughout the year means poorer-quality information for managers year-round, as well as longer times needed to prepare financial statements at year-end

61. At present, the government generally operates on a cash accounting basis throughout the year. Cash accounting recognizes only actual payments and receipts.

62. To prepare financial statements, after year-end the government converts accounting records that are on a cash basis to an accrual basis; accrual accounting recognizes revenue when earned or expenses when incurred, regardless of when cash actually changes hands. The conversion is a massive exercise, and is necessary because accrual accounting is required for financial statements.

63. For decision making throughout the year, accrual-based information is also better than cash-based information:

- The date that cash is received or paid does not necessarily bear any relationship to when a transaction occurs. For example, the government may pay a bill long after a good or service is received.

-
- When fully implemented, accrual-based accounting better considers when long-lived assets are used rather than when the government acquires them. For example, the government may construct a building that lasts for years. Managers can make better decisions when they know how much of the building's value is used or consumed each year; this usage is called "amortization" (formerly "depreciation").

64. Because the government generally operates on a cash accounting basis and the conversion to accrual accounting is time-consuming, throughout the year managers mainly rely on financial information based on cash accounting.

65. Organizations with better financial management and financial systems operate on a full accrual basis or very close to it year-round. As a result, they can prepare financial statements faster at year-end, and provide better information to managers throughout the year.

66. Certainly switching to accrual-based accounting throughout the year would be a major undertaking. However, we believe the switch is needed. In our view the appropriate time would be after addressing gaps in existing systems (Chapter 6) and structural problems with financial management (chapters 7 and 8).

67. Recommendation. The government should set a timetable for implementing accrual accounting at an appropriate date in the future.

Government response. The government agrees. A plan will be developed to fully implement accrual accounting in the future.

68. Legally required dates for tabling financial information.

Exhibit 4.1 summarizes requirements for tabling key financial information. In the case of both the interim report on the government's finances and a Crown corporation's annual report, the requirement is to submit the document to the responsible minister. In turn, the minister is required to table the report as soon as possible after receipt.

69. Actual tabling dates. It is simpler and more relevant to look at the dates documents are actually tabled. Exhibit 4.2 summarizes these dates, and the findings clearly show that MLAs and others are not receiving timely financial information about the government. Two reasons underlie the late tabling of financial statements:

- limited opportunities to table documents in the past
- problems in producing the financial statements and related information

Exhibit 4.1 Legally required dates for tabling key financial documents

Government's audited, consolidated summary financial statements

- Canada's *Nunavut Act* requires tabling by 31 December for the year ended the previous March. Nunavut's *Financial Administration Act* sets less stringent requirements. To comply with both acts, Nunavut must meet the federal requirement.

Government's interim financial report

- Nunavut's *Financial Administration Act* requires the Comptroller General (Deputy Minister of Finance) to submit the interim report to the Minister of Finance by the end of September, with tabling as soon as possible after receipt.

Crown corporations' annual reports (including audited financial statements)

- Nunavut's *Financial Administration Act* requires each Crown corporation to submit its annual report to the minister responsible within 90 days of year-end, or within 150 days of year-end if the Minister of Finance approves an extension. The minister responsible is required to table the report as soon as possible after receipt.

Exhibit 4.2 Actual tabling dates

Fiscal year	Month tabled	No. of months tabled after year-end	No. of months tabled after deadline
Government's audited, consolidated financial statements			
2003–04	December 2005	20	11
2002–03	May 2004	13	4
2001–02	June 2003	14	5
2000–01	May 2002	13	4
1999–2000	May 2001	13	4
Government's interim financial report			
2003–04	November 2004	7	N/A
2002–03	October 2003	6	N/A
Qulliq Energy Corporation / Nunavut Power Corporation, annual report			
2004–05	November 2005	7	N/A
2003–04	February 2005	10	N/A
2002–03	November 2003	7	N/A
Nunavut Housing Corporation, annual report			
2003–04	November 2005	19	N/A
2002–03	November 2004	19	N/A

Exhibit 4.2 Actual tabling dates (continued)

Nunavut Arctic College, annual report			
2003–04	February 2005	7	N/A
2002–03	May 2004	10	N/A
Nunavut Development Corporation, annual report			
2004–05	November 2005	7	N/A
2003–04	November 2004	7	N/A
2002–03	December 2003	8	N/A
Nunavut Business Credit Corporation, annual report			
2003–04	March 2005	11	N/A
2002–03	November 2004	19	N/A

Notes:

1. Legislation specifies a tabling deadline only for the government's audited, consolidated financial statements. In all other cases, the deadline specified is for submitting the document to the appropriate minister (Exhibit 4.1).
2. All tabling dates are from the Legislative Assembly's "Statutory Requirements for Tabling of Reports and Other Documents in the Legislative Assembly of Nunavut, November 2005," except for any tabling subsequent to the Second Session of the Second Legislative Assembly. Not included are any reports tabled after 16 December 2005.
3. The number of months from year-end is rounded down to the nearest whole month.
4. Nunavut Arctic College has a 30 June year-end. All others are 31 March year-ends.

Limited opportunities to table documents in the past

70. There have been dramatic changes in the time needed to table certain documents from one year to another (Exhibit 4.2).

71. The shifts could be due to the timing of Assembly sessions. A difference of a few days in the time taken to complete a report could advance or delay tabling by months.

72. Backdoor tabling. The Legislative Assembly recently amended its rules to allow documents to be considered tabled when the Assembly is not in session. Assembly officials indicate that when documents are tabled using this new approach, they will be provided immediately to MLAs and to others on request. On 16 December 2005, the government used this mechanism to table its 2003–04 audited, consolidated financial statements.

73. We hope that the government continues to take advantage of this opportunity to table financial information when the Legislative Assembly is not sitting for extended periods. It allows information to reach MLAs and others more quickly than in the past.

Problems in producing the actual financial statements and related information

74. Aside from limited tabling opportunities, financial information has been provided late because of delays in actually preparing and finalizing financial statements and other related documents, such as Crown corporation annual reports. The ability to produce financial statements quickly varies significantly from one government organization to another.

75. Dates of our audit reports for Nunavut's Crown corporations. Given that in the past there have been relatively few windows for tabling documents, the actual tabling dates do not clearly indicate whether financial information has been completed in a timely manner. The dates on our audit reports provide a better indication of timeliness.

76. After an audit report date, both the organization audited and our Office have much work to do to finalize and publish the financial information. However, since the audit report date represents a milestone in the work, it allows us to compare the timeliness of the overall process from year to year.

77. Our audit report dates for different Crown corporations demonstrate that some are doing much better than others in preparing financial statements on a timely basis.

- For 2002–03 and 2003–04 both Nunavut Arctic College and Nunavut Development Corporation produced good-quality draft financial statements within two months of year-end. As a result, we were able to complete much of our work and date our audit reports within two months of year-end as well.
- For 2002–03 and 2003–04 it took Nunavut Power Corporation / Qulliq Energy Corporation and Nunavut Business Credit Corporation much longer to produce good-quality draft financial statements. Consequently, our audit reports for these years are dated 5 or 6 months after year-end in most cases, and 19 months after year-end for Nunavut Business Corporation's 2002–03 fiscal year.

We commented on problems in both corporations in our 2004 report to the Legislative Assembly.

Exhibit 7.3 of this report notes problems that Nunavut Business Credit Corporation is experiencing in preparing its 2004–05 financial statements.

In the case of Qulliq Energy Corporation, we dated our 2004–05 audit report only four months after year-end, earlier than in the

past. While our opinion on Qulliq's 2003–04 financial statements contains an authorities reservation (Exhibit 2.3), our 2004–05 opinion on Qulliq is without reservation.

78. Nunavut's Crown corporations thus show dramatically varying ability to table their annual reports in a timely manner. This is an issue of importance to the entire government. To deal with it, the Crown Agency Council needs to continue monitoring Crown corporations' progress in providing timely annual reports to the Legislative Assembly. The Council also needs to continue working with individual corporations to improve timelines.

79. Recommendation. Through its Crown Agency Council, the government should continue to monitor the progress of Crown corporations in tabling their annual reports on a timely basis, and work with individual corporations to improve timeliness of the overall process.

Government response. *The government agrees. Letters of expectation were sent to the five major Crown corporations in May 2005. The letters clearly outlined requirements that these public agencies must follow with respect to daily operations, long-term planning, financial operations, and reporting. Responses to the letters were to be tabled during the November 2005 legislative session. A process has been put in place as a tool to help monitor compliance with these guidelines on an ongoing basis.*

Government's consolidated financial statements are a particular concern

80. Exhibit 4.2 presents tabling dates for all years for the Government of Nunavut's consolidated summary financial statements. The dates are of particular concern for two reasons.

81. First, the audited, consolidated summary financial statements are the only document that includes, or consolidates, financial information from all parts of the government. For this reason the statements are the most important financial information document prepared by the government at the end of a year.

82. Second, the government tabled the 2003–04 consolidated financial statements much later than for earlier years. Why is this the case?

83. Particular challenges in preparing the government's consolidated financial statements. There are three main steps in preparing Nunavut's consolidated summary financial statements. Each contributes to tabling delays.

-
- All departments need to complete their year-end accounting. Hundreds of individual tasks throughout departments and revolving funds need to be completed before the government can prepare its consolidated financial statements.

In the government's early days, accounting was much more centralized in the Iqaluit office of the Department of Finance than it is today. As a result, more year-end work was done in the Department itself, and it was easier to ensure that missing information was provided quickly.

- Crown corporations need to finalize their individual financial statements

The financial statements of all Crown corporations have to be reasonably final before the government can do the consolidation. We have noted that some Crown corporations require months to finalize their own financial statements.

- The Department of Finance needs to prepare the consolidated financial statements. We discuss this in following paragraphs.

What delayed tabling of the government's 2003–04 financial statements

84. Exhibit 4.3 lists milestones that help explain the extraordinary delays in tabling the government's 2003–04 financial statements. Preparing the financial statements involved four main steps: gathering information, preparing a draft, performing the audit, and translating the text.

- After year-end, the government took around nine or ten months to gather the bulk of the information needed for the Department of Finance to prepare the consolidated financial statements.
- The government took another three months to provide us with the first complete draft of the consolidated financial statements.
- We took around two months for our audit of the consolidated financial statements. (We earlier reviewed unconsolidated information from departments and we audited the financial statements of Crown corporations as information became available.) During this time the government reduced the reported annual surplus for 2003–04 by \$17 million to address errors we identified.
- The process of Inuktitut translation took around five months.

85. Tabling of the 2003–04 financial statements was unduly delayed for two reasons: a bottleneck within the Department of Finance, and delays in translation.

Exhibit 4.3 Milestones in preparing the government's 2003–04 consolidated financial statements

Month	Months after year-end	Milestone
Late 2004 / early 2005	9–10	Information from Crown corporations needed for consolidation was generally available.
April 2005	12	We received first incomplete draft of consolidated financial statements.
May 2005	13	We received first complete draft of consolidated financial statements.
During our audit work	13	The government reduced the surplus it reported in its draft financial statements by \$17 million to correct significant errors we noted during our audit.
May 2005	13	Date of our auditor's report.
June 2005	14	Auditor General signed auditor's report.
July 2005	15	We completed our review of the consolidated financial statements in English, and provided permission for the government to use the Auditor General's audit report in English.
July 2005	15	We received a first draft of the consolidated financial statements in Inuktitut for our review.
September 2005	17	We informed the government that there were significant differences between the final English and draft Inuktitut consolidated financial statements, requiring correction.
November 2005	19	We received a second draft of the consolidated financial statements in Inuktitut for our review.
November 2005	19	We informed the government that there were still significant differences between the final English and second draft Inuktitut consolidated financial statements, requiring correction.
December 2005	20	Differences between English and Inuktitut versions were resolved. Financial statements were made public in both Inuktitut and English by filing with the Legislative Assembly.

86. Bottlenecks in preparation of financial statements. Senior governments in Canada, including the Government of Nunavut, use public-sector accounting rules. Some of these differ from the private-sector rules with which most professional accountants in Canada are familiar. In September 2005, in our view only three accountants within the Department of Finance had experience with these special rules.

87. The peak workload in preparing the consolidated financial statements began when the bulk of information was available around January 2005 and ran until June 2005. Throughout this period, two of

the three staff with the necessary detailed knowledge had other main duties. One of them applied for and was appointed to a job unrelated to preparing financial statements. The second was serving as an acting Assistant Deputy Minister, with duties far broader than financial statements.

88. Delays with Inuktitut translation. Exhibit 4.3 shows that the government spent around five months working on Inuktitut translation of the 2003–04 financial statements. This includes time during which we reviewed the translation and reported errors to the government.

89. Recommendation. The government should ensure that appropriate technical resources such as accountants with specialized knowledge and Inuktitut translators are available at key times to allow the financial statement process to move along smoothly.

Government response. The government agrees. The government will increase its efforts to ensure that appropriate resources are available for this purpose.

Why the government has never met its 31 December statutory deadline for the consolidated financial statements

90. If the government is to meet its statutory deadline for tabling its consolidated financial statements, all stages of preparation need to be completed much sooner. This is necessary to allow time for audit, translation, and printing before 31 December.

91. In many cases tasks would need to be completed months earlier to meet deadlines. Since the government has not significantly advanced reporting dates over six years, a breakthrough would be needed to table the consolidated financial statements by the end of December each year.

92. The late tabling of financial statements is really a symptom of the weak and fragile state of the government's financial management. Until the government solves numerous financial management problems, we are not optimistic that it can meet the deadline for completing and tabling its consolidated financial statements.

93. This is yet another reason to improve financial management. In our view, the key is to remove structural barriers to such an improvement (chapters 6 and 7). Only this will allow the government to table its consolidated financial statements significantly earlier.

Chapter 5

Other financial statement issues

94. This chapter examines financial information issues other than the delays discussed in Chapter 4. We first look at outstanding issues mentioned in previous reports, and then raise a new issue related to Crown corporations.

Outstanding issues from our previous reports

95. Our previous reports raised two important issues:

- The government's audited, consolidated financial statements do not record environmental liabilities.
- Readers cannot compare the government's financial plans to actual results.

96. Both issues are still unresolved.

97. **The government's audited, consolidated financial statements do not record environmental liabilities.** A healthy environment is vital to all Nunavummiut. There are two important reasons for a government to record environmental liabilities in its consolidated financial statements.

- First, if the government has not already done so, the process of recording such liabilities requires it to identify and assess environmental damage, and to determine who is responsible for cleanup.
- Second, cleanup costs could be huge or minimal. Until the assessment work is complete, there is no way of knowing.

98. We first reported this issue in our 2001 report to the Legislative Assembly. In its response to our recommendation the government agreed to complete the work, but indicated that it could take over five years.

99. In its 2003–04 consolidated financial statements the government notes that the work is under way.

100. Meanwhile, accounting standards for Canadian governments are evolving. A new accounting standard is in effect from 2005–06. This new standard puts added pressure on governments to record environmental liabilities in their consolidated financial statements.

101. Recommendation. The government should complete its ongoing assessment of environmental damage in time to allow recording of environmental liabilities, if any, in its 2005–06 financial statements.

Government response. The government agrees. It has been working with the federal government to complete this assessment since 2001, but the results will not be ready in time for liabilities to be recorded in the 2005–06 financial statements. The government will increase its efforts to complete the assessment as soon as possible.

102. Readers cannot compare the government’s financial plans to actual results. A comparison of budgets to actual financial results is a fundamental tool used by readers of financial statements to evaluate performance. In Nunavut’s case, readers need to compare the government’s fiscal plans set out in the main estimates to actual financial results in the audited, consolidated financial statements.

103. At present, they cannot do so. Exhibit 5.1 explains why.

104. Paragraph 63 explains why using amortization to account for long-lived assets gives a truer picture of the government’s operations. Exhibit 5.1 notes that the consolidated financial statements use amortization, while the main estimates do not. In our view, the way to solve the problem is by adjusting the main estimates, not the audited, consolidated financial statements.

105. We reported this issue previously. In response to a related recommendation in our 2004 report to the Legislative Assembly, the

Exhibit 5.1 Plans and results: Two reasons why the government’s main estimates (plans) cannot be compared to audited, consolidated financial statements (results)

Consolidated financial statements versus unconsolidated main estimates

Consolidated financial statements include information on Nunavut’s Crown corporations, while unconsolidated financial statements include information only on departments and revolving funds. Nunavut’s Crown corporations are an important part of the government’s operations, and spend and collect large amounts of money on the government’s behalf. Only consolidated information properly reflects the total size of the government.

The government’s audited financial statements are consolidated. The main estimates are not.

Different treatment of capital assets

In accordance with accounting rules for senior governments in Canada, the government’s audited, consolidated financial statements spread out the cost of capital purchases over the life of an asset. This practice is called amortization or depreciation.

However, the main estimates show the entire cost of a capital purchase as an expense in the year of purchase. Amortization gives a better picture of the government’s operations (paragraph 63).

government agreed to move to accrual-based budgeting as soon as practicable. While this would deal with the issue of the different treatment of capital assets, in its 2004 response the government was silent on how it planned to deal with the issue of consolidated versus unconsolidated information.

106. Until the government solves both these issues, readers of its consolidated financial statements cannot compare budgets to actual results.

107. Recommendation. The government should set a specific fiscal year by which it will solve the ongoing problem that financial statement readers cannot compare actual results to the government's plans.

Government response. The government agrees. The Department of Finance has established a Senior Fiscal Advisor position to take the lead in the conversion to accrual-based budgeting. Accrual-based budgeting is projected to be implemented by 31 March 2008.

Nunavut Crown corporations must deal with complex new accounting standards in 2005–06

108. In response to recent accounting scandals around the world, new standards make it harder for an entity to avoid reporting unfavourable financial news by transferring losses to another entity.

109. The new rules apply to Nunavut's Crown corporations starting from 2005–06. There are three points to consider:

- Each corporation will have to review its operations to see whether the new rules apply.
- If the new rules are applicable, the corporation will have to adopt a completely different method of accounting for its interests in third parties.
- The work involved could be very difficult.

There could be significant duplication of effort if each Crown corporation separately attempts to assess the implications of the new standards.

110. The government provides financial leadership to Crown corporations through its Crown Agency Council. Given the complexities, the Council needs to help Crown corporations deal with the new standards.

111. Recommendation. Through its Crown Agency Council, the government should provide leadership in helping Nunavut's Crown

corporations to assess the impact of new accounting standards relating to interests in third parties. If the new standards apply, the government should also provide leadership in helping the Crown corporations implement the new standards by the 2005–06 deadline.

Government response. *The government agrees. The Department of Finance will provide guidance on the standards relating to interests in third parties.*

Chapter 6

Duplications and gaps in the government's accounting systems

Efforts to improve financial management have yielded few results

112. We are convinced that government officials have made significant efforts to improve financial management and deal with other problems noted in our earlier reports. Despite that, progress has been slow. Why is this so?

113. In our view, the ways in which the government's accounting systems and financial management structure are set up are significant barriers to improvement.

114. This chapter examines barriers created by the government's accounting systems. Chapter 7 examines barriers created by financial management structures.

The government's computerized accounting systems

115. We reviewed the government's systems as part of our financial statement audit. Our audit is not specifically designed to draw conclusions on the quality of systems, and would not usually identify all matters of interest to management or members of the Legislative Assembly. Nonetheless, the following observations may be helpful to the government as it determines how to achieve rapid improvements in financial management.

116. Complexity of computer systems normally related to size and complexity of organization. Normally there is a relationship between the size of an organization and the kind of accounting systems it needs and uses. A small organization may be able to function without computerized systems, or with informal systems developed by users or simple pre-packaged accounting software designed for home computers.

117. The government has over \$1 billion in assets, spends over \$1 billion a year, and has some 2,300 employees in departments alone. As a large and complex organization, it needs appropriate systems to support its operations.

Financial systems vary

118. The heart of a computerized accounting system is a general ledger. This pulls together financial information from various sources. It also allows information to be generated for use in helping managers manage and in preparing financial statements.

119. Other computer modules may handle specific functions, such as payroll, purchasing, inventory, revenue and accounts receivable, and expenses and accounts payable. Still other components may deal with unique aspects of an organization. The government's current accounting systems raise a number of issues.

120. Crown corporations use a variety of systems differing from those of departments. The government provides payroll services to three Crown corporations. Two others, however, have their own pay systems, and all Crown corporations operate their own separate main accounting systems.

121. The level of independence of the Crown corporations' finances has actually increased since the creation of the Government of Nunavut. The Nunavut Business Credit Corporation (NBCC) is the territory's smallest Crown corporation, with only a handful of employees. At first a government department used the government's main financial system to do NBCC's accounting. Later, when NBCC headquarters moved out of Iqaluit, a controller was hired for the Corporation, and it adopted its own general ledger system differing from that used by departments.

122. Nunavut's Crown corporations vary in size and complexity of operations. Perhaps not all of them ought to use the same systems as departments. However, different systems make it more difficult to ensure the quality of financial management and financial data for the entire government. In addition, the government needs information from all the systems to prepare its consolidated financial statements, which include all the Crown corporations.

123. Recommendation. The government should review the appropriateness of continuing to allow all Crown corporations to operate their own main financial computer systems.

Government response. *The government agrees. The operation by Crown corporations of their own main financial computer systems will be reviewed by the Department of Finance in consultation with the Crown corporations and any affected government departments.*

124. Gaps exist in formal systems. In government departments, some important financial management functions use relatively unsophisticated systems, or duplicate systems are used elsewhere if no central systems exist. Exhibit 6.1 gives some examples.

125. Widespread reliance on informal manual and spreadsheet systems. Informal spreadsheet systems are widely used within the government. This is a concern to our Office. More formalized accounting systems have controls built into them to reduce risks of error or fraud. It may be possible to build some basic controls into informal manual and spreadsheet systems, but doing so requires a good understanding of system design. It also takes time.

126. When informal spreadsheets become important parts of financial systems, there are other risks as well. For example, if key information is kept on an individual's personal computer, are backups completed regularly? Is there adequate security? If the person leaves, will others be able to access and understand the information?

Exhibit 6.1 Examples of relatively unsophisticated or duplicated systems

Manual leave records

The government still maintains manual leave records, despite having some 2,300 employees. As noted in paragraph 13, around 50 percent of leave records we reviewed contained errors.

Management informs us that a new personnel system being implemented is capable of generating automated leave records.

No main loans accounting system

The government's main accounting system lacks a loans accounting module. Managers have instead developed spreadsheet systems for areas such as student loans and municipal loans.

No main inventory systems

The government's main accounting system lacks an inventory module. The Petroleum Products Revolving Fund and the Liquor Revolving Fund have the largest inventories in the government. In the absence of a main inventory module, both use their own separate inventory systems.

No main purchasing or contract systems

The government's main accounting system lacks a purchasing or contract module. This makes it harder to manage and account for purchases of all sizes in the government.

Management informs us that a purchasing system is under development.

Specialized areas use manual records or spreadsheets for information

The government has thousands of transactions a year for medical travel and income support. At present, it tracks these payments through a combination of manual and spreadsheet-based systems instead of regular accounting systems. Management informs us that a system for tracking medical travel is under development. An earlier attempt to introduce a system for tracking income support was unsuccessful.

127. Finally, how does the government know that information maintained in informal systems is accurate and complete?

128. The government has duplicated basic accounting systems in different parts of its organization—a situation that we recommend be reviewed.

129. At the same time, some systems we would expect to see in an organization of the government's size are missing, or operated as informal manual systems or spreadsheets, thereby increasing the risk of error or fraud.

130. Both situations interfere with the government's attempts to put acceptable financial controls in place.

131. **Recommendation.** The government should identify and address gaps in formal computer systems used for key accounting and financial management functions.

Government response. *The government agrees. It will initiate a review of systems currently used for key accounting and financial management functions in 2006–07.*

Chapter 7

Structural barriers to improving financial management

A decentralized structure

132. Exhibit 7.1 summarizes the government’s accounting structure in terms of where transactions are processed. Accounting systems and practices are highly decentralized. That is, accounting staff are scattered throughout departments and regions, often working in small units.

133. A recent survey found that the government has 196 accounting positions (from clerks to directors), most of which are outside of Iqaluit (Exhibit 7.2).

Implications of decentralization

134. There are four key implications of Nunavut’s highly decentralized accounting structure. Together they suggest the underlying reasons for Nunavut’s inability to rapidly improve its financial management.

- A decentralized accounting structure requires a higher proportion of experienced professional accountants. Nunavut does not have enough professional accountants to meet its needs given the existing structure.
- Financial management gains in one area come at the expense of losses in another.
- It is difficult to deploy accounting resources to where they are most needed.
- Training for the future may suffer in the current decentralized structure.

We will examine each of these points in detail.

Exhibit 7.1 Where the government does its accounting

- **Departments and regions** usually do their own processing of non-payroll expenses.
- All **Crown corporations** have their own accounting systems, each with a different general ledger system from that used by the Department of Finance.
- The Department of Finance provides **payroll services** to departments, revolving funds, and three Crown corporations: Nunavut Arctic College, Nunavut Housing Corporation, and Nunavut Business Credit Corporation.
- Qulliq Energy Corporation and Nunavut Development Corporation process their own payroll.

Exhibit 7.2 Where are the people who do the accounting located?

	Department of Finance	Other departments	Total
Iqaluit	29	65	94
Outside Iqaluit	24	78	102
Total	53	143	196

Source: Government of Nunavut initial survey of accounting jobs from clerks to directors, September 2005.

Numbers cited are for positions, some of which are vacant. The government's figures include the Nunavut Housing Corporation but not other Crown corporations since from time to time the government groups the Housing Corporation with departments when reporting government-wide information.

Nunavut does not have enough professional accountants to meet the needs of its decentralized accounting structure

135. Professional accountants defined. A professional accountant generally is a university graduate and has one of the three Canadian recognized accounting designations: CA (chartered accountant), CGA (certified general accountant), or CMA (certified management accountant).

136. Large and complex organizations such as the Government of Nunavut generally have a number of professional accountants to guide accounting and financial management.

137. Nunavut's current decentralized accounting structure requires more professional accountants than it now has if the government is going to make the existing structure work.

138. For six years the government has tried to improve financial management, with little success. It needs people with experience and professional expertise to develop solutions.

139. At the same time, Nunavut's highly decentralized accounting structure forces people in the many accounting groups to work more independently. That takes a greater presence of experienced and professional accountants who can work on their own, oversee and mentor others, ensure the quality of financial information, and interpret and report information produced by accounting systems.

140. The government reports that it has 196 accounting positions in departments and the Nunavut Housing Corporation (Exhibit 7.2), of which 166 are filled. In November 2005 a survey found that the government has 27 professional accountants currently working in departments and the Nunavut Housing Corporation, or 16 percent

of total accounting staff. However, while the majority of accounting positions are outside Iqaluit, only 30 percent of the government's professional accountants are based outside the capital. The government also notes that it has at least nine employees studying toward professional accounting designations.

Financial management gains in one area come at the expense of losses in another

141. For a number of reasons, the government faces significant challenges in hiring more professional accountants and other trained staff needed to bring about rapid improvements in financial management.

142. First, obtaining a professional accounting designation requires study and experience. It will take years to train Land Claims Agreement beneficiaries and others for senior accounting roles. In the meantime, there is a desperate need to improve financial management.

143. Second, there are difficulties in hiring experienced professional accountants from elsewhere in Canada. The problems include a hot job market nationally and stiff competition for staff housing in Nunavut.

144. Many accounting vacancies in Nunavut are filled by hiring someone already working as an accountant elsewhere in the government. One part of the government gains, while another part loses.

It is difficult to deploy accounting resources to where they are most needed

145. The government's accounting forces are divided. Under Nunavut's *Financial Administration Act*, ultimate responsibility for financial management in the government lies with the Department of Finance. However, only about a quarter of accounting positions are within that department (Exhibit 7.2).

146. This is a problem because of the fragility of the government's current accounting. At present, a single employee's departure or transfer can seriously harm accounting in part of the government. In this situation the government needs flexibility so that it can move accounting talent rapidly to where it is most needed. Impeding flexibility is the fact that most employees in accounting positions work for individual departments and cannot be transferred out of those organizations.

147. Exhibit 7.3 describes some recent bottlenecks in accounting. Recentralization (Chapter 8) would give more flexibility to

accounting functions and would help deal with bottlenecks. Until it happens, the government needs to see whether it can develop a mechanism for rapidly moving accounting staff across its organization to deal with changing needs.

Exhibit 7.3 Examples of bottlenecks in the government's accounting

Department of Finance

Paragraph 87 notes that there was a shortage of staff with the necessary skills when it came time to prepare Nunavut's 2003–04 consolidated financial statements.

Department of Economic Development and Transportation, and Department of Health and Social Services

Because accounting is so decentralized in the government, the Department of Finance relies on departments, revolving funds, and Crown corporations to provide much of the information it needs to prepare the audited, consolidated financial statements.

Departments were supposed to submit their 2004–05 information no later than July 2005. In September 2005 the two departments had still to supply considerable information. Their slowness created delays in both the Department of Finance's accounting work and our early audit work.

Liquor Revolving Fund

The Government of the Northwest Territories provided accounting services for Nunavut's Liquor Revolving Fund until October 2004. The accounting was then transferred to the Government of Nunavut in Rankin Inlet. The plan was to use the government's main accounting system to record expenses and purchases, and a personal computer-based accounting system to record the \$4 million of annual sales and inventory. Ultimately, however, sales and inventory transactions need to be entered in the government's main accounting system so that master accounting records are complete.

Despite this, the sales and inventory information was not recorded in the government's main accounting system for the remainder of the fiscal year, and the personal computer-based system and the government's main system were never reconciled. In late September 2005 accounting information was transferred to the Department of Finance's Government Accounting Division in Iqaluit to complete the work needed to prepare financial statements for the Revolving Fund's 2004–05 fiscal year.

Nunavut Business Credit Corporation

Nunavut's smallest Crown corporation has only a handful of employees. In March 2005 the Corporation's controller left the government. By the following October the position had not been filled.

The Corporation has struggled to prepare its 2004–05 year-end financial statements. In May 2005 we did what audit work we could. In November 2005 we received the first draft financial statements of sufficient quality to allow us to resume our work.

148. Recommendation. The government should seek short-term options for rapidly moving accounting resources where they are needed across departments and Crown corporations to deal with changing needs.

Government response. Although the government agrees with this objective, it has been difficult to achieve in the past and will continue to be in the

foreseeable future because of ongoing resourcing constraints. The Department of Finance plans to fill two Senior Fiscal Advisor positions in 2006–07 in order to provide additional accounting-related support for departments and Crown corporations.

Training for the future may suffer in the current decentralized structure

149. Training Land Claims Agreement beneficiaries for accounting jobs is important, both to contribute to Nunavut's commitments under the Agreement and to prepare beneficiaries for increasing responsibility in the future. For several reasons we are concerned that on-the-job training may not be effective in Nunavut's decentralized accounting structure.

150. First, in chapters 2, 3, and 4 we note situations in which the government is not following laws. Lack of familiarity with the law is part of the problem. It also means that staff with supervisory responsibilities may themselves lack knowledge or information needed to carry out their jobs well.

151. Second, we note heavy work demand in certain positions (Exhibit 7.3). Individuals with high workloads may lack the time needed to train others.

152. Third, with many small accounting units throughout Nunavut, staff may not have exposure to a sufficient variety of tasks to prepare them for more senior duties. For example, junior accounting clerks may mainly process and file expense vouchers. If they have no growth opportunities, they will find it difficult to move to more senior jobs with much more varied tasks and responsibilities.

Chapter 8

Improving financial management today and tomorrow

153. Chapters 1 to 5 of our report provide numerous examples of problems with the government's financial management, including lack of proper approval for 10 percent of payments, errors in about 50 percent of leave records, a record of spending money before approval, and a chronic inability to provide information to the Legislative Assembly on time.

154. In order to have basic financial controls, the government needs to master six broad areas. While financial management is better today than when Nunavut was created, the government is not yet doing well enough in any of the six areas (Exhibit 1.1).

155. Just as worrisome is the fact that we have reported nearly all of these issues or similar ones to the Legislative Assembly in the past.

156. Chapters 6 and 7 describe structural problems with the government's financial systems and decentralized services. These have foiled the government's efforts to improve financial management.

157. Having analyzed the problems, in this concluding chapter we recommend ways of breaking through the barriers in order to improve the government's financial management now and for the future.

158. Both short- and longer-term solutions are needed for

- improving financial management now
- ensuring that beneficiaries of the Nunavut Land Claims Agreement are prepared for senior financial management jobs in the future

Improving financial management now

159. To improve its financial management as soon as possible, the government has three broad options.

- Option 1: Fine-tune existing systems

The easiest course is to make changes within existing systems. This has been tried for six years, with very limited success. We do not think that it will work.

-
- Option 2: Keep existing accounting systems and add professional accountants to make them work

In Chapter 7, we note that the government does not have sufficient professional accountants for its current needs.

It might be possible to make existing systems work by adding a significant number of experienced professional accountants to solve the problems that have arisen and prevent new ones from occurring.

In the short term, this would mean hiring individuals from southern Canada—something not easy to do given the current strong demand for accountants elsewhere. Also, out-of-territory recruitment would add to competition for staff housing. Last, hiring more accountants would make the government's financial management even more expensive.

We do not think this option is practical.

- Option 3: Change the financial management system

In our view, this is the only realistic option. It would involve some form of recentralization of accounting jobs to solve the problems noted in Chapter 7.

160. Recommendation. To achieve breakthroughs in financial management, the Government of Nunavut should recentralize certain accounting operations. In doing so, the government needs to make key decisions, including how to structure recentralized functions and how far to go toward a centralized accounting structure.

Government response. The Government of Nunavut is aware of this issue and has recently initiated "The Review of GN Financial Structures Project." The purpose of this review is to analyze internal financial capacity and recommend a detailed plan for improving the Government of Nunavut's ability to plan, control, and forecast expenditures, and to enhance the timely and accurate production of the Public Accounts. A final report is scheduled to be delivered by 31 March 2006. The scope of the review includes the assessment of government-wide financial management capacity to effectively manage and account for resources in the following areas: risk management and control, information, and management of resources.

161. We understand and respect the government's right to establish policies for Nunavut, including the decentralization policy. We are not in any way criticizing existing policies. We feel that accounting functions can be recentralized in a manner that respects these policies.

162. With this in mind, the government would need to decide how to structure recentralized accounting functions, and how far to go toward a centralized approach.

163. Recentralization could free money for other uses. From discussions with officials we understand that the government is looking for different ways of doing business to save money for use in other areas, such as housing or fuel prices.

164. The government estimates that it has 196 accounting positions in departments and the Nunavut Housing Corporation. Of these it estimates that about 166 were actually filled in September 2005. The government also reports that in June 2005 it had 2,387 positions filled in departments and the Nunavut Housing Corporation. This means that about seven percent of the government's employees worked in the accounting support function.

165. Usually governments seek to lower costs for support functions in order to have as much money as possible for programs that directly help people.

166. If Nunavut recentralizes accounting functions, it could achieve efficiency gains from bringing workers together. As a result, it might lower its future accounting costs. At the same time, dealing with other issues discussed in this report is likely to require new government expenditures. For example, filling gaps in accounting systems (Chapter 6) will necessitate spending to implement the new systems.

167. Recentralization could provide better training for Land Claims Agreement beneficiaries. We appreciate the need to train beneficiaries of the Nunavut Land Claims Agreement. This is essential to fulfill obligations under the Agreement and to provide high-quality jobs for beneficiaries.

168. We believe that larger work groups can offer better training opportunities, preparing beneficiaries to handle more senior jobs. In larger work groups, supervisors may have more time for training and mentoring. In addition, beneficiaries who currently hold more junior accounting jobs may be exposed to a wider variety of tasks, preparing them for advancement.

169. Recentralization need not conflict with the government's decentralization policy. We are aware that decentralization is important to the government and Nunavummiut. Depending on how it is handled, recentralization of accounting functions could conflict with government policy. But this need not be the case.

170. There are various ways of recentralizing accounting operations:

- Centralize all accounting functions under one roof

At one extreme, the government could handle all its accounting functions at a single site. This would reduce accounting jobs at other locations.

- Form larger work groups throughout Nunavut

Under this model, units in different parts of Nunavut would continue to process transactions. However, individual work groups would become fewer and larger.

- Create centres of excellence

Under this model the government would create centres of excellence in different parts of Nunavut to handle different specialized accounting functions. One office might process payroll for all of Nunavut, another office located elsewhere might handle other types of payments, and a third office might process revenue.

These are only examples, and it is up to the government to choose the model it will follow. However, we need to add a note of caution: Six years of tinkering with financial management has not produced necessary improvements. Recentralization needs to be reasonably bold or it might not work at all.

171. Recentralization could give the government greater latitude.

Recentralization could reduce the total number of accounting jobs needed, and give the government latitude for managing the change in structure.

172. For example, savings could be used to fund other jobs in communities affected, in order to maintain overall decentralization of government. Savings could also be used for other government priorities, or for unexpected requirements. It is the government's choice.

173. Recentralization would not affect services to the public. Finally, the shift we are suggesting would not affect jobs requiring direct interaction with the public. Most accounting jobs are relatively invisible to the public. Visible service jobs do not have to be moved to improve financial management.

174. In fact, recentralization should improve services overall. Better financial management would give the government access to more timely, accurate information. At the same time it would reduce the risk of errors, bad decisions, and fraud. That would benefit all Nunavummiut.

Ensuring that Land Claims Agreement beneficiaries are prepared for senior financial management jobs in the future

175. An opportunity for beneficiaries. Many financial management jobs are complex and require considerable experience and training. The Government of Nunavut will always require professional accountants for certain jobs. In our view, the government needs to ensure that beneficiaries of the Nunavut Land Claims Agreement have the opportunity to become professional accountants.

176. Building on other successes. The government's success in producing Inuit lawyers has been widely reported throughout Canada, and Nunavut is justifiably proud of this achievement.

177. To ensure good financial management and train beneficiaries for more leadership roles in the future, the government needs to develop programs to produce Inuit professional accountants.

178. For some time the government has had programs to train junior and mid-level accounting staff. While the programs benefit the government, the training needed to become a professional accountant is fundamentally different and takes years of formal education.

179. We understand that the Department of Finance is exploring options for beneficiaries to study for university degrees in commerce or related areas. This would be a good start; a university degree is normally a milestone on the path to becoming a professional accountant.

180. Recommendation. The government should develop training programs that will help Land Claims Agreement beneficiaries to become professional accountants and develop other senior-level financial management skills.

Government response. The government agrees. The Department of Finance will continue with efforts to train beneficiaries for more senior accounting and financial management positions. Also, it will establish a comprehensive human resources development plan to strengthen financial management capabilities.

Conclusion: Good financial management for good government

181. After six years of slow progress, we recommend that the Government of Nunavut now take decisive action to improve financial management. Good financial management will reduce the risk of error, bad decisions, and fraud. It will help provide good government to all Nunavummiut.

Appendix A About our audits and the Office of the Auditor General of Canada

Our vision

The Office of the Auditor General is an independent audit office serving the Legislative Assembly and the people of Nunavut. It is widely respected for the quality and impact of its work.

We promote:

- accountable government
- an ethical and effective public service
- good governance
- sustainable development
- the protection of Nunavut's 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 of Nunavut, and Nunavummiut;
- working with other 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 *Nunavut Act*, section 46(1), we audit the accounts and financial transactions of the Government of Nunavut to express an opinion on the government's consolidated financial statements.

Our audits include reviews of certain operating, legislative, and financial control systems, and financial management practices, with detailed tests as we consider necessary.

This *Report of the Auditor General to the Legislative Assembly of Nunavut*, also known as the Report on Other Matters, is part of our audit. In accordance with the *Nunavut Act*, section 46(2), the Auditor General is to report on any other matters arising from the audit that should be communicated to the Legislative Assembly. 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. The matters reported were noted during our financial and compliance audits of the consolidated financial statements and Crown corporations.

Readers should be aware that the primary purpose of our audits is to express an opinion on the financial statements. Consequently, our audits will not identify all issues that may be of interest to members of the Legislative Assembly or others.

Exhibit A.1 shows where our audit reports contain “reservations” to highlight significant issues with the financial statements, compliance with authorities, or other key issues.

Exhibit A.1 Our recent audit opinions¹

Entity	Year ended	Audit report date	Reservations to audit opinion?	Date tabled
Government of Nunavut (consolidated)	31 March 2003	24 March 2004	Yes ²	21 May 2004
	31 March 2004	24 May 2005	Yes ²	16 December 2005 ³
Nunavut Arctic College	30 June 2003	19 September 2003	No	19 May 2004
	30 June 2004	27 August 2004	No	28 February 2005
	30 June 2005	9 September 2005 (except Note 10, dated 2 December 2005)	No	Not yet tabled
Nunavut Business Credit Corporation	31 March 2003	7 November 2003 (except Note 13, dated 3 September 2004)	Yes ²	30 November 2004
	31 March 2004	3 September 2004	Yes ²	18 March 2005
Nunavut Development Corporation	31 March 2004	25 June 2004	No	30 November 2004
	31 March 2005	28 June 2005	No	18 November 2005
Nunavut Housing Corporation	31 March 2003	31 October 2003	No	25 November 2004
	31 March 2004	17 September 2004	No	23 November 2005
Qulliq Energy Corporation	31 March 2004	13 October 2004	Yes ²	25 February 2005
	31 March 2005	3 August 2005	No	29 November 2005
Workers' Compensation Board of the Northwest Territories and Nunavut	31 December 2002	28 March 2003	No	30 November 2004
	31 December 2003	26 March 2004	No	3 March 2005
	31 December 2004	25 February 2005	No	21 November 2005

¹ Listed here are audits tabled since our last report to the Legislative Assembly, as well as audits not yet tabled.

² For details of reservations, see Chapter 2.

³ This is the date filed with Legislative Assembly (paragraph 72)

Our people

Many people with different skills and experiences carry out an audit. Together these resources allow the Office to make a difference. Since Nunavut is large, our audit work involves staff from our Ottawa, Edmonton, and Montréal offices. Many of the staff work on Nunavut audits only as brief assignments.

Assistant Auditors General		
Ron Thompson Andrew Lennox		
Principals		
Dale Shier, Ottawa Roger Simpson, Edmonton		
Staff		
Chantal Archambault	David Irving	Minh-Duc Nguyen
Marie-Noëlle Beauchamp	Mary-Jo Jacksic	Mila Simon
Sylvie Cossette	Tyleen Kearney	Robin Webb
Darlene Holloway	Guy Legras	Peter Yeh

Reporting and management comments

Our Office policy requires audit observations and recommendations to be referred to the management of the audited organizations for comment. Where appropriate, the Office obtains management's written responses to recommendations in audit chapters.

We provided our draft chapters to the Office of the Comptroller General of Nunavut, government departments, and Crown corporations, where appropriate. Government responses are included in the relevant chapters.

Our thanks

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

For information, please contact Communications at (613) 995-3708 or 1-888-761-5953 (toll-free).

Appendix B Summary of our recommendations and management responses

The following is a list of recommendations found in this report. The number in front of the recommendation indicates the paragraph where it appears in the report. The numbers in parentheses indicate the paragraphs where the topic is discussed.

Recommendation	Government response
Chapter 1	
17. While manual leave records remain in use, the government should continue training to reduce errors. (13-16)	The government agrees. Additional training will be provided as required.
27. The government's Internal Audit Services Branch should review all major cost-sharing agreements to identify opportunities for faster billing and collection. (22-26)	The government agrees. The Department of Finance will be working closely with other Government of Nunavut departments to ensure that they disclose all major cost-sharing agreements, and identify opportunities for faster billing and collection. In addition, there will be quarterly reporting of cost-sharing agreements to improve disclosure and collection.
<hr/> Chapter 2	
40. To ensure that employees with financial responsibilities can do their jobs, the government should continue training them to be aware of all necessary authorities. (37-39)	The government agrees. It will continue to hold information sessions on key Financial Administration Manual directives.
41. To monitor progress in reducing payments made without proper approval, the government should continue internal audit work on signing authorities. (37-39)	The government agrees. The work of the Internal Audit Services Branch will continue, including audits and training sessions.
47. The government should disclose debt for purposes of the debt cap in its 2004–05 audited, consolidated financial statements. (42-46)	The government agrees. This information will be included in the 2004–05 audited financial statements.
50. The government should develop procedures for monitoring the debt cap throughout the year. (48-49)	The government agrees. A Treasury function is being established in the Department of Finance, and will be operational for the 2006–07 fiscal year. Part of this function will be to monitor and report the Government of Nunavut's debt on a quarterly basis.

Recommendation	Government response
Chapter 3	
<p>57. The Government of Nunavut should take immediate steps to ensure that it asks the Legislative Assembly for approval of spending in advance rather than after the fact. (53-56)</p>	<p>The government agrees. It has implemented procedures to ensure that departmental appropriations are sufficient to fund expenditures and that approval is sought prior to actual spending of public funds. These procedures include enhancement of the budget variance report process and strengthening person-year controls. The government will continue to strengthen financial controls in this area.</p>
Chapter 4	
<p>67. The government should set a timetable for implementing accrual accounting at an appropriate date in the future. (61-66)</p>	<p>The government agrees. A plan will be developed to fully implement accrual accounting in the future.</p>
<p>79. Through its Crown Agency Council, the government should continue to monitor the progress of Crown corporations in tabling their annual reports on a timely basis, and work with individual corporations to improve timeliness of the overall process. (74-78)</p>	<p>The government agrees. Letters of expectation were sent to the five major Crown corporations in May 2005. The letters clearly outlined requirements that these public agencies must follow with respect to daily operations, long-term planning, financial operations, and reporting. Responses to the letters were to be tabled during the November 2005 legislative session. A process has been put in place as a tool to help monitor compliance with these guidelines on an ongoing basis.</p>
<p>89. The government should ensure that appropriate technical resources such as accountants with specialized knowledge and Inuktitut translators are available at key times to allow the financial statement process to move along smoothly. (84-88)</p>	<p>The government agrees. The government will increase its efforts to ensure that appropriate resources are available for this purpose.</p>

Recommendation	Government response
Chapter 5	
<p>101. The government should complete its ongoing assessment of environmental damage in time to allow recording of environmental liabilities, if any, in its 2005–06 financial statements. (97-100)</p>	<p>The government agrees. It has been working with the federal government to complete this assessment since 2001, but the results will not be ready in time for liabilities to be recorded in the 2005–06 financial statements. The government will increase its efforts to complete the assessment as soon as possible.</p>
<p>107. The government should set a specific fiscal year by which it will solve the ongoing problem that financial statement readers cannot compare actual results to the government’s plans. (102-106)</p>	<p>The government agrees. The Department of Finance has established a Senior Fiscal Advisor position to take the lead in the conversion to accrual-based budgeting. Accrual-based budgeting is projected to be implemented by 31 March 2008.</p>
<p>111. Through its Crown Agency Council, the government should provide leadership in helping Nunavut’s Crown corporations to assess the impact of new accounting standards relating to interests in third parties. If the new standards apply, the government should also provide leadership in helping the Crown corporations implement the new standards by the 2005–06 deadline. (108-110)</p>	<p>The government agrees. The Department of Finance will provide guidance on the standards relating to interests in third parties.</p>
Chapter 6	
<p>123. The government should review the appropriateness of continuing to allow all Crown corporations to operate their own main financial computer systems. (118-122)</p>	<p>The government agrees. The operation by Crown corporations of their own main financial computer systems will be reviewed by the Department of Finance in consultation with the Crown corporations and any affected government departments.</p>
<p>131. The government should identify and address gaps in formal computer systems used for key accounting and financial management functions. (124-130)</p>	<p>The government agrees. It will initiate a review of systems currently used for key accounting and financial management functions in 2006–07.</p>

Recommendation	Government response
Chapter 7	
<p>148. The government should seek short-term options for rapidly moving accounting resources where they are needed across departments and Crown corporations to deal with changing needs. (145-147)</p>	<p>Although the government agrees with this objective, it has been difficult to achieve in the past and will continue to be in the foreseeable future because of ongoing resourcing constraints. The Department of Finance plans to fill two Senior Fiscal Advisor positions in 2006–07 in order to provide additional accounting-related support for departments and Crown corporations.</p>
Chapter 8	
<p>160. To achieve breakthroughs in financial management, the Government of Nunavut should recentralize certain accounting operations. In doing so, the government needs to make key decisions, including how to structure recentralized functions and how far to go toward a centralized accounting structure. (159)</p>	<p>The Government of Nunavut is aware of this issue and has recently initiated “The Review of GN Financial Structures Project.” The purpose of this review is to analyze internal financial capacity and recommend a detailed plan for improving the Government of Nunavut’s ability to plan, control, and forecast expenditures, and to enhance the timely and accurate production of the Public Accounts. A final report is scheduled to be delivered by 31 March 2006. The scope of the review includes the assessment of government-wide financial management capacity to effectively manage and account for resources in the following areas: risk management and control, information, and management of resources.</p>
<p>180. The government should develop training programs that will help Land Claims Agreement beneficiaries to become professional accountants and develop other senior-level financial management skills. (175-179)</p>	<p>The government agrees. The Department of Finance will continue with efforts to train beneficiaries for more senior accounting and financial management positions. Also, it will establish a comprehensive human resources development plan to strengthen financial management capabilities.</p>