



Office of the Auditor General of Ontario

# Annual Report *2016*



*Volume 1 of 2*



## 6.0 Significant Accounting and Reporting Issues

### 6.1 Consolidation of Hydro One and Ontario Power Generation

PSAB standards direct government business enterprises (GBEs) to follow the accounting rules applicable to publicly accountable enterprises and prepare their financial statements using International Financial Reporting Standards (IFRS) effective for the fiscal year beginning on or after January 1, 2011. IFRS is the Canadian generally accepted accounting principles applicable to these enterprises.

Three of the five GBEs that are consolidated by the Province report financial results under IFRS as required by PSAB standards (i.e., Brampton Distribution Holdco Inc, Liquor Control Board of Ontario and Ontario Lottery and Gaming Corporation). The other two GBEs, Hydro One and Ontario Power Generation (OPG), do not report under Canadian generally accepted accounting principles (i.e., IFRS) and instead have used U.S. generally accepted accounting principles (U.S. GAAP) since 2012.

The transition to U.S. GAAP was brought about by the Ontario Regulation 395/11 which the government passed in response to the decision made by the Chartered Professional Accountants of Canada (formerly the Canadian Institute of Chartered Accountants) Accounting Standards Board (AcSB) to adopt IFRS for all publicly accountable enterprises. At the time, U.S. GAAP had provisions to cover the accounting by corporations whose rates are regulated by an independent, third party regulator, but IFRS did not. The use of rate regulated accounting is under review by both the AcSB and the International Accounting Standards Board (IASB). Rate regulated accounting is discussed in further detail later in this report.

The AcSB had issued multiple extensions to rate-regulated organizations to allow them to continue

to use the “pre-changeover accounting standards” (i.e., former Canadian GAAP prior to adoption of IFRS) that included provisions for rate-regulated accounting up to January 1, 2015.

Since 2012/13, even though Hydro One and OPG have been using U.S. GAAP for their stand-alone financial statements, these financial statements have been converted to the former Canadian GAAP for inclusion in the Province’s consolidated financial statements.

In January 2014, the IASB issued an interim IFRS standard that permits first-time adopters of IFRS to continue their previous GAAP accounting for regulatory deferral account balances, with limited presentation changes. This interim IFRS standard was effective for annual periods beginning on or after January 1, 2015.

Hydro One and OPG both have December 31 fiscal year-ends. The Province’s accounting policy is to adopt in-year accounting policy changes to the next full provincial fiscal year. As such, the Province continued to consolidate Hydro One and OPG in the 2014/15 fiscal year based on the results under the former Canadian GAAP.

We examined the differences between IFRS and the former Canadian GAAP at the time and concluded that the estimated differences had no material effect on the annual deficit.

Recognizing that the government was choosing to continue to use U.S. GAAP and not IFRS for consolidation of the financial results of OPG and Hydro One in the Province’s consolidated financial statements, we requested and received from OPG and Hydro One’s attest auditors, through specified procedures, the differences for 2015/16 between U.S. GAAP and IFRS. We relied on their work for consolidation purposes.

In February 2016, the Treasury Board Secretariat wrote CPA Canada’s Accounting Oversight Committee and PSAB requesting that the PSAB standards recognize U.S. GAAP as a basis of reporting by publicly accountable enterprises because the current standards only refer to IFRS. The government noted that by excluding reference to other

sources of GAAP, PSAB mandates that GBE results must be reflected on an IFRS basis. The government expressed concern that this could result in materially different and inconsistent results in the Province's consolidated financial statements than if the rate regulated entities (Hydro One and OPG) results were consolidated on a U.S. GAAP basis. PSAB responded in July 2016 that the PSAB standards would not be changed and all GBEs should prepare their financial statements in accordance with IFRS and not U.S. GAAP.

Despite the response, with the former Canadian GAAP no longer being an option, the government chose to consolidate Hydro One and OPG results under U.S. GAAP in 2015/16 as opposed to consolidating them on an IFRS basis, as required under PSAB standards. We examined the differences between IFRS and U.S. GAAP accounting standards, highlighted by Hydro One and OPG attest auditors, and concluded that these estimated differences had no material effect on the annual deficit. We recorded these differences on our summary of unadjusted audit differences. In addition, we requested that the Province disclose these differences. It disclosed this information in Note 12 to its Consolidated Financial Statements.

We will continue to track these differences in subsequent audits until the government adopts IFRS for the purposes of consolidating the results of OPG and Hydro One, as required. Given the differences in how certain balances are treated under U.S. GAAP versus IFRS, we anticipate that these differences could become material in future fiscal years, potentially as soon as the 2016-17 fiscal year.

## RECOMMENDATION 6

We recommend that the Province of Ontario include Hydro One and OPG financial information in the consolidated financial statements using the IFRS reporting framework as required by PSAB standards.

## TREASURY BOARD SECRETARIAT RESPONSE

Treasury Board Secretariat will continue to work with the Public Sector Accounting Standards Board and the Office of the Auditor General to ensure that the Province's financial reports support transparency and accountability to the public and other users.

## 6.2 Contaminated Sites

A new PSAB standard came into effect for the fiscal year ending March 31, 2015. It requires the province's liability for contaminated sites to be updated to incorporate any changes that have occurred during each fiscal year.

Examples of changes that would affect the liability estimate include:

- identification of new sites where contamination may exist and assessment, remediation and monitoring may be required;
- additional remediation work performed on existing sites; or
- new information that becomes available about a site following more in-depth assessments or the advent of new technology.

As part of our Public Accounts audit for fiscal year ending March 31, 2016, we examined the liability for contaminated sites and the changes that occurred throughout the fiscal year. The liability balance as at March 31, 2015, was \$1.792 billion, which decreased to \$1.751 billion as at March 31, 2016. Although there were some new accruals added, the majority of the change is due to amounts spent to remediate sites, which lowered the liability.

We also reviewed sites that were not included in the estimate to ensure the criteria for recognition and disclosure under the PSAB standard were appropriately assessed. We agreed with the relevant ministries' conclusion for not including these specific sites since the PSAB criteria were not met. The ministries will monitor these sites for any changes in the future that may have an effect on the liability for contaminated sites.