AUDITOR GENERAL

1994/95: Report 5

Compliance-with-Authorities Audits

Elevating Devices Safety Act

Travel Agents Act

Financial Administration Act: Guarantees and Indemnities

Land Tax Deferment Act

Compliance–with–Authorities Audits

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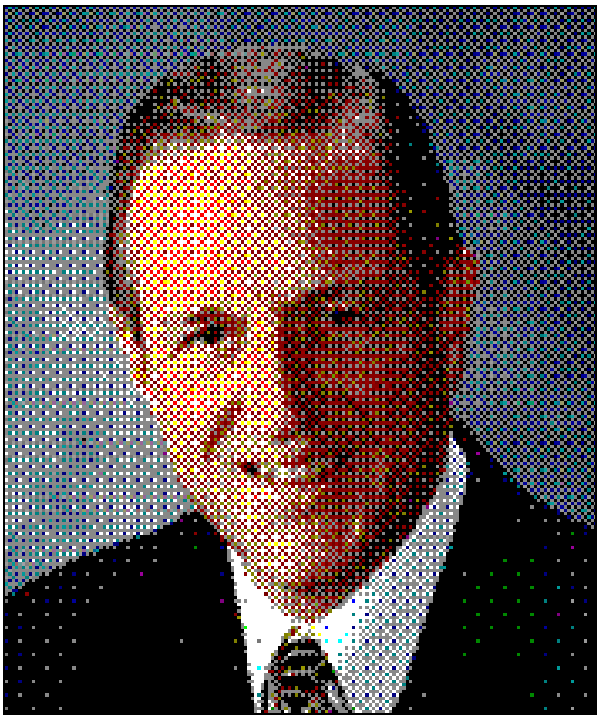


This is my fifth report to the Legislative Assembly for 1994/95, and it is a report on the compliance–with–authorities audit work performed by my staff during the past year.

Four such audits were conducted, and we also obtained updated responses from government officials as to actions taken by them with respect to prior years' audit recommendations which had been endorsed by the Select Standing Committee on Public Accounts.

Our compliance–with–authorities audits for 1994/95 dealt with four distinct statutes of the Province, as follows:

- the *Elevating Devices Safety Act* and related regulation, which set out rules to ensure the safe operation of elevating devices;
- the *Travel Agents Act* and related regulation and policy, which regulate the operation of travel agents in British Columbia, and the Travel Assurance Fund;
- the *Financial Administration Act* (sections 56 to 58), the Guarantees and Indemnities Regulation and the related Treasury Board policies, which provide for the approval, control, and reporting of guarantees and indemnities; and
- the *Land Tax Deferment Act*, which enables eligible property owners to defer payment of their property tax.

Our audit of the guarantees and indemnities sections of the *Financial Administration Act* is a continuation of our ongoing, cyclical, compliance–with–authorities auditing of this Act, which is the government's principal legislation governing financial administration, control and reporting.

While we found that the *Land Tax Deferment Act* was being complied with in all significant respects, we had reservations about the extent of compliance with the other three statutes and their related authorities. Consequently, the detailed report sections that follow have recommendations for improvements, which I trust will be well considered by the officials concerned.

The appendices at the end of this report provide a listing of compliance–with–authorities audits completed from 1990 to date, and an outline of the audit objectives and methodology employed in conducting these audits.

I wish to acknowledge the outstanding work undertaken by my staff, which has resulted in the production of these reports, and to thank them for their professional dedication and application. I also greatly appreciate the cooperation shown to my staff by the officials and staff in the ministries and other government organizations into which these audits took us.

George L. Morfitt, FCA
Auditor General

Victoria, British Columbia
May, 1995

Elevating Devices Safety Act

Elevating Devices Safety Act

The* Elevating Devices Safety Act *and related regulation set out rules to ensure the safe operation of elevating devices.

Audit Report

Audit Scope

We have made an examination to determine whether certain significant sections of the *Elevating Devices Safety Act* and related regulation were being complied with, in all significant respects, as of August 1994; specifically, those relating to:

- filing plans and specifications for elevating devices;
- inspection before use;
- annual operating certificates;
- periodic inspections;
- tests of safety gear;
- contractor licencing; and
- reporting of accidents.

Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

Audit Opinion

In our opinion, the sections of the *Elevating Devices Safety Act* and related regulation requiring the follow up of government directions for corrective action arising from periodic inspections, and the testing of safety gear every three years, were not being satisfactorily complied with as of August 1994; whereas the remaining sections of the Act and related regulation that we examined were being satisfactorily complied with, in all significant respects, as of August 1994.

Introduction

The *Elevating Devices Safety Act* and the *Elevating Devices Safety Regulation* provide for the safe operation of "elevating devices," the majority of which are elevators and escalators, but also include handicapped lifts, amusement rides, construction hoists, and other similar devices, as shown in Exhibit 1.1. The Act requires that the contractors who design, construct, install, alter, repair, maintain and test the devices be licenced, that each device be registered, and that each device be inspected on a periodic basis by a ministry inspector.

The Act is administered by the Boiler and Elevator Safety Branch of the Safety Engineering Services Division of the Ministry of Municipal Affairs.

The Act and regulation establish the following requirements for the design, construction, installation, alteration, repair, testing, and operation of elevating devices:

- the plans and specifications for new devices, or significant alterations of existing devices, must be filed with the Branch;
- an elevating device must comply with the applicable safety codes;
- an elevating device must be inspected before it is licenced for use;
- an elevating device must have an annual certificate to operate;
- an elevating device must be inspected on a periodic basis once it is licenced for use;
- tests of certain kinds of safety gear (activated by overspeed sensors, usually found on traction elevators) must be done every three years;

Elevating Devices

As of July 1994, there were almost 14,000 elevating devices operating in the Province, and another 400 under construction. Over the last five years, an average of 700 new devices have been installed each year. The most common device is the passenger elevator, accounting for almost 80% of the total, of which over 70% are situated in the Lower Mainland.

Apart from special devices, elevators operate in one of two ways: they are either suspended from above or supported from beneath. Elevators suspended from above are typically powered by an electric hoist motor, and have a counterweight, often set at 40% of the maximum rated weight of the car and passengers. The counterweight reduces the load on the motor. Elevators with overhead traction have safety gear consisting of a brake which operates on guide rails at the side of the hoist shaft. The brake is activated by an overspeed sensor, and brings the elevator to a stop if it descends too quickly. Approximately 5,000 of this type are installed in British Columbia.

Elevators supported from beneath are powered by a hydraulic ram. These elevators do not have the same safety gear as do overhead traction devices. Instead the coupling to the ram is sized to limit the speed with which the hydraulic fluid can be pumped into or out of the ram, thus providing a physical limit to the speed of descent should a break in the hydraulic lines occur. Generally, hydraulic elevators are used in buildings of up to five stories. There are about 6,500 of this type in British Columbia.

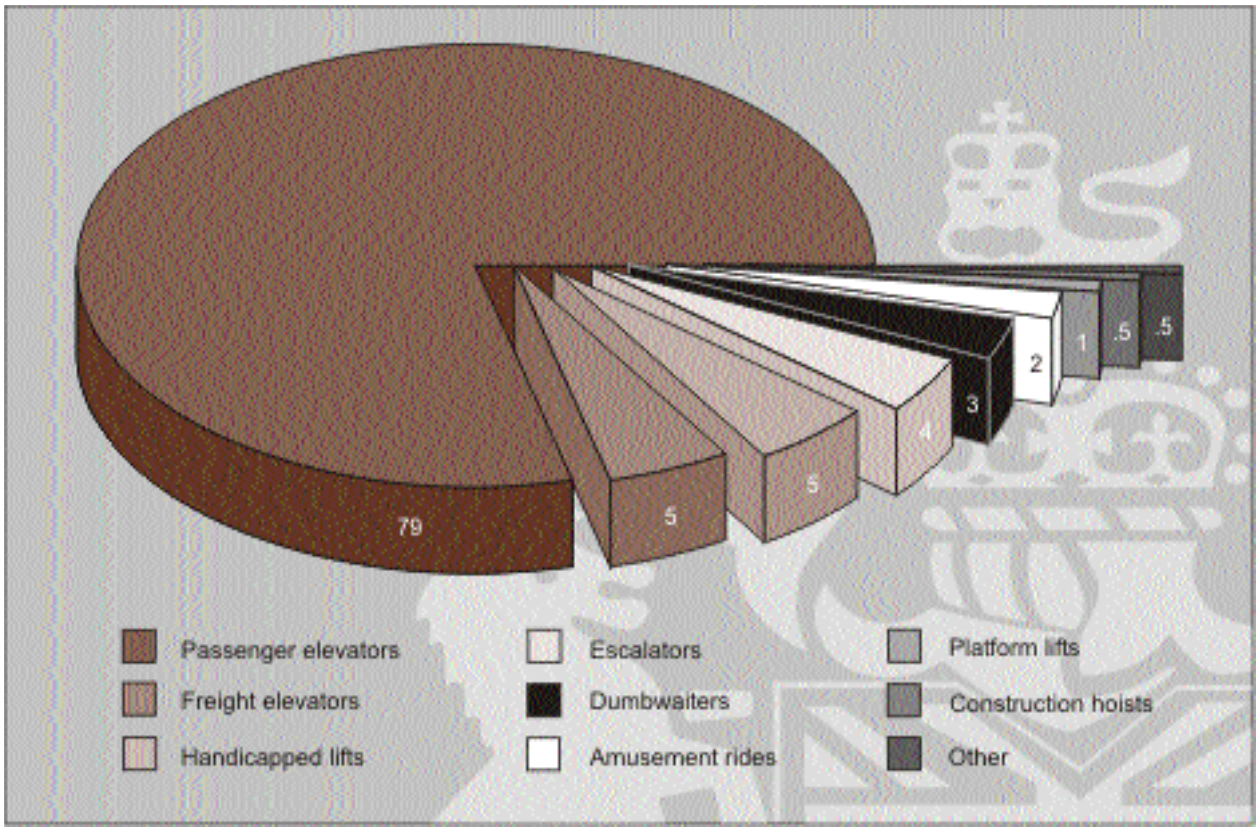
- contractors who design, construct, install, alter, repair, maintain, and test devices, must be licenced;
- operators, where needed to operate a device, must be licenced; and
- accidents must be reported to the Branch.

Elevating devices are owned by the individuals, groups or corporations that own the buildings (or midways, for amusement rides, etc.), and those owners are responsible for their correct and safe operation. All work concerning the devices must be carried out by licenced contractors.

Before construction of a new device begins, or before a significant alteration is made to an existing device, the contractor must file the engineering drawings of the device with the Branch. As well, the contractor must certify that the device will conform with the requirements of the Act and regulation, and thus with the appropriate safety codes

Exhibit 1.1

Different Types of Elevating Devices (Comparison by %)



Source: As of July 31, 1994, based on records at the Boiler and Elevator Safety Branch

(Exhibit 1.2). At this time, a unique identifying number is assigned to the device.

Once the device has been constructed and installed, the contractor calls for an acceptance inspection. This is carried out by the contractor and witnessed by the ministry inspector. Tests are performed to confirm the correct functioning of the device, including the operation of the safety gear, as well as matters relating to the construction of the elevator shaft and machine room, such as the existence of a minimum clearance between the top of the elevator and the top of the shaft. However, the inspector cannot verify that the device complies with all the applicable safety codes – for example, that the device was in fact built using the proper materials and construction and welding techniques.

An elevating device must pass the acceptance inspection before it is allowed to operate. Once it has passed, decal plates inscribed with the device number are affixed to it.

When a device is in operation, the owner must purchase an annual certificate to operate. In addition, the device must be inspected by a ministry inspector on a periodic basis, "a regular inspection," although the legislation does not specify when or how often. To ensure the continuing safe operation of the different kinds of devices, the Branch has an unwritten policy that all devices should be inspected at least once every three years, with amusement rides being inspected at least annually and construction hoists at least monthly.

The Act also requires that specific safety gear, which is operated by overspeed sensors and is most commonly found on traction elevators, be tested once every three years. Getting this test done is the responsibility of the owner, but the job of a contractor. The latter provides an affidavit detailing the result of the test to the Branch.

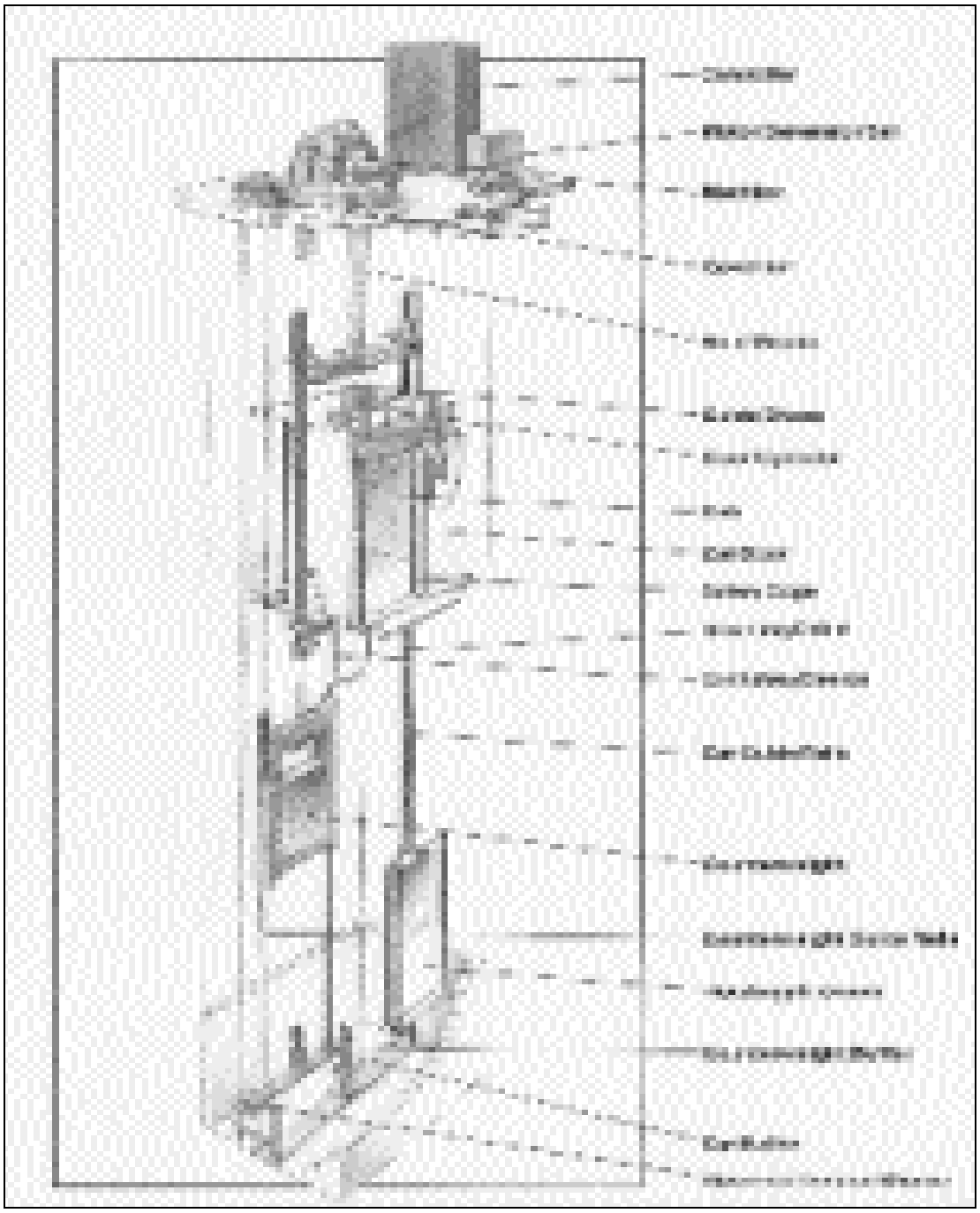
Following either an acceptance or a regular inspection, an inspector may issue directions concerning matters that have been found that are not in accordance with the Act, regulation, or safety

Exhibit 1.2

Safety Codes and Standards

The Canadian Standards Association publishes safety codes and standards for various products in Canada. The *Elevating Devices Safety Regulation (schedule B)* specifies the standards that must be followed, including specific codes for elevators and escalators, as well as more general codes dealing with such topics as electrical equipment and metal arc welding. These codes specify types of material that can be used, design factors of safety, safe operation and control, and other safety items.

A device must comply with the safety codes that are in force at the time it is constructed. Revisions to the safety codes are made to improve safety. Generally, devices do not have to be upgraded to meet the requirements of the new codes, unless mandated by the inspection authority or voluntarily modernized by the owner.



Schematic of an elevator

codes. These directions can cover anything from changing the hoisting ropes to installing an appropriate caution sign on the machine room door. Depending on the seriousness of the matter, the inspector can take the elevator out of service until the directions have been completed (and advise the public by means of a notice affixed to the device). Alternatively, where safety is not the issue, the inspector can allow a time period of up to 90 days for their completion,

depending upon the severity of the matter, while allowing the device to remain in operation in the meantime. The owner is required to notify the Branch in writing when the directions have been completed. Once a device has been taken out of service, a further inspection is required before the device can be put back into service.

The owner of an elevating device must report to the Branch all accidents that result in injury or death. Fatal accidents must be reported immediately and the device shut down. Injury accidents must be reported within 24 hours. If the safety gear engages, that must also be reported within 24 hours. After being notified of an accident, the Branch and contractor make a site investigation to establish the cause.

Contractors must be licenced by the Branch. Approximately 290 licenced contractors are currently in the Province. Persons wishing to be licenced as contractors must submit an application to the Branch, and then go through a panel review process. Different classes of licence can be applied for and issued. For example, a contractor may be licenced to work on only one type of device, or may be restricted to doing maintenance rather than design, construction and installation. The licence must be renewed annually. A contractor's qualifications can be reviewed at any time if events warrant.

Some elevating devices require an operator, who must be licenced by the Branch. An operator controls the functions of the device, such as opening and closing the doors on an elevator, ascending and descending, and stopping level with the floor outside. There are approximately 800 licenced operators in the Province, the majority of whom operate construction hoists and elevators in high–rise buildings approved for manual operation during the final phases of construction. As well, a few heritage buildings have elevators that require operators. Persons wishing to get licenced are interviewed by the Branch, and must have received instruction in the operation of the particular device from a licenced contractor. Operators' licences must be renewed annually.

Audit Scope

Our audit was conducted to determine whether certain significant sections of the *Elevating Devices Safety Act* and related regulation were complied with, in all significant respects, as of August 1994. Specifically, we audited for compliance with those sections requiring that:

- the plans and specifications for devices be filed at the Branch;
- all elevating devices be inspected before being licenced for use;
- all elevating devices have annual certificates to operate;
- all elevating devices be inspected on a periodic basis;
- the tests of safety gear, as specified in the regulation, be done every three years;
- contractors be licenced; and
- accidents be reported within the specified time period.

We reviewed Branch records for about 200 elevating devices and 32 contractors, selected at random. We also had discussions with Branch personnel, and performed other tests and analyses that we considered necessary to determine whether the various requirements of the Act and regulation were complied with.

We included all types of elevating devices that come under the Act. These include passenger and freight elevators, handicapped lifts, escalators, and other devices as shown in Exhibit 1.1.

Some sections of the Act and the regulation we did not audit for compliance, including the standards and safety codes governing the safe construction and operation of elevating devices, and investigations into accidents. We also did not review the operations of the Elevating Devices Appeal Board (which hears appeals against decisions of the director of the Branch), or the Elevating Devices Advisory Committee (which advises the Minister on all matters of safety related to elevating devices), and neither did we review the licencing of operators.

The Act and regulation do not apply to elevating devices on property owned by the federal government or by First Nations peoples. In addition, certain devices, as specified in section 2 of the Act, are exempted. These include elevating devices in private residences (occupied by one person or family unit), devices used in mines or for agricultural purposes, coin operated amusement rides, portable elevating devices for persons with physical disabilities, and a number of other types of ramps and hoists.

Overall Observations

We found that:

- properly prepared plans and specifications for elevating devices have been filed at the Branch;
- elevating devices in the Province to which the Act and regulation apply have been licenced by the Branch;
- elevating devices are receiving acceptance inspections prior to being allowed to operate, although the Branch does not obtain assurance that the elevating device has been built in accordance with the Act, regulation and safety codes;
- elevating devices have annual certificates to operate;
- about one fifth of elevating devices are not being inspected with the frequency that the Branch considers necessary, although there is nothing in the legislation, beyond the word “periodic,” as to what that frequency should be;
- owners are not notifying the Branch consistently that directions issued as a result of inspections have been carried out, and the Branch has been inconsistent in following up those outstanding directions;
- tests of the safety gear, where required, are not always being done at least every three years;
- elevating device contractors are properly licenced;

- although there is no planned review of all contractors' performance at the time they apply for the renewal of their licences, the competency of contractors is reviewed when exceptions or infractions are noted; and
- accidents are generally reported within the specified time period, except for the reporting of accidents involving amusement rides.

We also found that regular maintenance of elevating devices is not a requirement of the Act or regulation, although we were informed that approximately 80% of elevating devices are covered by maintenance contracts.

Audit Findings

Filing of Plans and Specifications with the Branch

The contractor must file plans and specifications with the Branch for a new device and for any significant alteration of an existing device. The plans must be prepared and sealed by a professional engineer, and the application that accompanies them must be signed by the contractor, thereby certifying that the device will meet the standards of the Act, regulation, and applicable safety codes. This filing is the first step in the licencing process.

We looked to see whether there was a record of the filing of plans and specifications for each device in our audit sample. Records of the initial filing of 35 devices constructed before 1970 were not available, but we did not otherwise find any omissions.

Licencing of Devices

We also wanted to determine whether all devices in the Province subject to the Act had been licenced. Any device not licenced is not included in the database at the Branch, and so is not inspected or monitored to ensure that safety tests are performed, if applicable.

We found that the Branch does not actively seek out information about newly installed devices. Instead, it expects the contractors to comply with the regulation and file plans for all new elevating devices in the Province. However, it does receive some information from various sources about devices that may not be licenced, and these are investigated.

We visited Vancouver, Victoria, and other communities on Vancouver Island to look at some devices. We checked to see that they all had a unit number affixed or engraved, and recorded the location of the device. We then checked the record at the Branch for each unit number to verify that the devices had been licenced.

All the devices in our sample proved to be correctly numbered and licenced.

As well, we recorded the location of a number of construction sites for new high–rise buildings and, where appropriate, noted whether there was a construction hoist present. We then looked to see if plans had been filed for devices to be installed in those buildings, and whether there was a construction hoist recorded as being at that location.

For all sites but one, we found that plans had been correctly filed.

In that one case, construction had not yet started, so filing was not required at that time. We also found that Branch records located construction hoists at the sites where we saw them.

Elevators and escalators are the most common devices in the Province, accounting for over 88% of the total. We consider that municipal building inspection departments are in the best position to know what new construction is occurring in the Province, and therefore where new elevators and escalators are being installed. We spoke to the building inspection departments in five municipalities throughout the Province to find out if there was any communication between them and the inspectors or the Branch about the locations of new buildings with elevating devices in them. We found that there was no such communication. One municipality stated that it asked for a copy of the acceptance inspection certificate (issued by a Branch inspector, but provided to the municipality by the building owner) before issuing a certificate of occupancy for the building.

We concluded that the Act is being complied with, in all significant respects, in its requirements for the licencing of devices.

However, we recommend that the Ministry of Municipal Affairs discuss with municipalities the possibility of having them either require a copy of the acceptance inspection certificate before issuing a certificate of occupancy, or inform the Branch when a permit is issued for a building that contains an elevating device.

Acceptance Inspections

A device must pass an acceptance inspection, performed by a contractor and witnessed by a ministry inspector, before it can be put into service. This inspection includes making sure that all of the controls function properly, verifying and documenting that the safety gear works as it should, checking the clearance between the car of the elevator and the top and bottom of the shaft in accordance with the safety code, measuring the speed of the device under full and no–load situations to ensure it is within the design parameters, and other similar technical matters. Whereas a regular inspection may take one or two hours, an acceptance inspection may last a day or more. In the last four years, the Branch has carried out an average of 1,015 acceptance inspections each year.

From time to time, a new class of elevating device will be brought under the provisions of the Act. Usually, some of the devices in question will already be in operation. For example, there were a number of stage lifts operating in the Province before it was decided that stage lifts should be classified as an elevating device and brought under the Act. Such devices did not have to cease operation before the acceptance inspection was performed.

We found that all the devices in our audit sample had undergone an acceptance inspection, before being allowed to operate. In some cases the actual record of the inspection was not available because of the disposal of documents, but other information

collected during the acceptance inspection was on file.

We noted that the Branch does not require an affidavit or similar document from the contractor after an elevating device has been built, certifying that it was in fact built in accordance with the Act, regulation, and safety codes. Tests by the inspector are referenced in specific sections of the code and include observations of the operation of the device and a visual inspection of it. Some aspects of the safety code, such as those that relate to the design specification and construction technique (proper welding, for example), cannot be tested in this fashion. However, where the building is a "part 3" building according to the British Columbia Building Code (generally, a building in excess of 6,000 square feet, more than four stories high, or serving as a place of public assembly), we found that municipalities, in accordance with the Building Code, require a "Schedule C Assurance of Professional Field Review and Compliance" from the architect. This confirms that the building and any elevating devices in it have been constructed according to the appropriate codes.

We recommend that the Branch, as part of the acceptance inspection, require some form of written assurance from the contractor that the device has been constructed in accordance with the Act, regulation and safety codes.

Annual Certificate to Operate

The Act requires all elevating devices to have an annual certificate to operate. The certificates are obtained from the Branch, on payment of the appropriate fee. The Branch sends out a renewal invoice to the owner of the device three months before the expiry date.

We found that all of the devices in our sample had annual certificates, although 22 had been renewed after the expiry date (on average, one month later) and, at the time of our audit, the renewals on three devices were three weeks overdue. One of these overdue licences was paid the week after our audit, but the other two were paid 12 and 15 weeks later.

We concluded that the Act was being complied with, in all significant respects, in its requirement that a device have an annual certificate to operate.

However, we noted that obtaining an annual certificate is simply a matter of paying the appropriate fee. There is no requirement, or checking, to ensure that a device is up–to–date on safety tests.

We recommend that the Branch require an affidavit that the safety tests required by the regulation are up–to–date before it renews the annual certificate to operate.

Regular Inspections

Regular inspections involve a visual examination of all the exposed parts of a device and the related safety gear. The normal functioning of the device is observed and the equipment in the machine room is inspected. Included are such things as ensuring that the correct fuses are used, that the elevator stops level with the floor, any cables used to support the elevator are not frayed or worn, that the emergency alarm

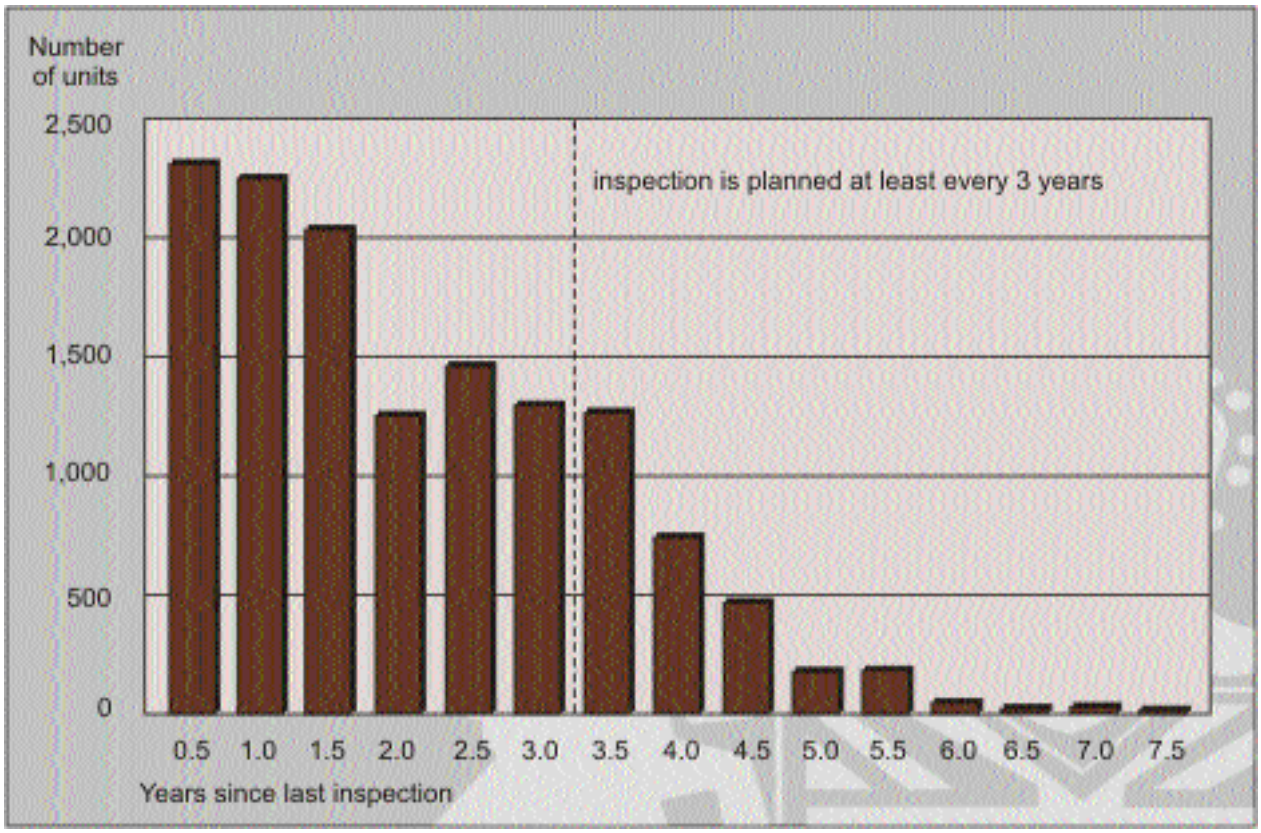
works, that the doors will not close if someone is in the way, and other matters of proper operation. An average of 3,588 regular inspections has been done in each of the past four years.

The regulation calls for the director to cause every device to undergo periodic inspection. "Periodic" is not defined in the regulation. We were told by Branch officials that the intent is to have each elevating device inspected at least once every three years, except for construction hoists which are to be inspected at least every month, and amusement rides which are to be inspected at least once each year. In addition, since 1993, an inspector has been in full time attendance while the Pacific National Exhibition midway is in operation during the summer.

Our tests found that 156 devices, or 77% of our sample (excluding those in our sample that were not in use), had been inspected within the last three years, and 49 devices, or 23% of our sample, had not. The Branch's own records indicate that approximately 20% of devices have not been inspected in the past three years. Exhibit 1.3 shows the time that has

Exhibit 1.3

Number of Years Since Last Inspection (excluding amusement rides and construction hoists)



Source: As of July 31, 1994, based on records at the Boiler and Elevator Safety Branch

elapsed since devices were last inspected, where the maximum permissible interval between inspections is three years.

Although we found that all the amusement rides in our sample had been inspected within the past year, the Branch's records showed that approximately 39% of amusement rides had not. This represents 115 devices. We did a further review on 54 of these, selected at random. We found that 27 of these had been shut down or moved out of the Province and 6 had been inspected recently but the Branch's records had not yet been updated. In the end, therefore, we found only 6 amusement rides that had not been inspected but should have, and a further 15 that had not been inspected that were of the permanent waterslide type. Although this indicates there is not a significant problem, it also shows that the Branch records are not up–to–date.

As well, we found that although all the construction hoists in our sample had been inspected within the previous month, the Branch's records seemed to show that the majority had not. According to Branch records, 17 had been inspected within the last month and 75 had not. However, when we looked into the hoists that had not been inspected, we found that the problem was that the records were not up–to–date. Either the hoists were not currently in use, or an inspection had been done within the last month but not yet recorded.

We concluded that elevating devices are not being inspected as often as the Branch intends them to be. However, since the regulation only requires "periodic" inspection, we are unable to say that the regulation is not being complied with.

We recommend that the maximum permissible interval between inspections of elevating devices be specified in the regulation or policies.

We recommend that the Branch update its records to reflect the correct operational status of amusement rides and construction hoists.

We noted that the Branch has no checklist of regular inspection procedures. Instead, inspectors rely on their knowledge, experience, and training to ensure that they cover all points. The Branch has considered developing a checklist in the past, but instead encourages the inspectors use their judgement rather than restricting them to the procedures listed on a checklist.

Given the sheer volume of safety code requirements, we understand the need for ensuring inspectors have flexibility in applying their judgement. However, we also believe that a checklist would help define and document the minimum inspection requirements, and that it would not in any way limit an inspector's prerogative to do or check whatever is necessary in the circumstances.

We recommend that the Branch draw up a checklist to document the minimum important procedures that must be performed during an inspection.

Infractions Found by Inspectors

Infractions found by inspectors are recorded on the inspection

reports as directions to the owner. These directions require that some action be taken within a certain time period, and the regulation requires the owner to notify the Branch in writing when the directions have been carried out. A re–inspection will not necessarily follow. In situations where safety is the issue, the inspector may decide that the device must be shut down until the directions are completed. In these cases, a notice is affixed to the device by the inspector and a re–inspection, at least of the matter that caused the problem, is done before the device is returned to service.

Directions were issued on 157 out of 190 inspections in our audit sample. In only 34 cases was there a notification from the owner or contractor on file that the directions had been completed, and in 9 of those the directions had been completed later than required by the inspector. In the other 123 instances, there was no notification that the directions had been done, and no record in the file of a follow–up by the inspector.

The Branch indicated that this was more of a paperwork issue than a serious operational issue. It said that if there was an immediate safety concern, then the device would be shut down (and would be required to be re–inspected before being put back into use). We were told that it is common for an inspector to be in contact with the same contractor about a number of different units within a few days, and often the inspector will receive verbal notification that the problem has been resolved. However, there was no documentation in the files we examined to indicate this.

In those cases where the Branch had not been notified that directions had been completed, we also reviewed the previous inspection report. We found that in only six instances were the directions on the most recent report a repeat of those, if any, on the previous report. This implies that in all the other 117 instances the previous directions had been carried out, even though the Branch had received no notification.

We concluded that the regulation covering notification to the Branch of completion of directions is not being complied with. Although it appears that directions may be completed at some point in the period between inspections, we could not verify this.

We recommend that the Branch develop procedures for following up with owners who have not notified it, as required by the legislation, to ensure that the directions have been carried out.

Tests of Safety Gear

The regulation requires owners of elevating devices which have specific safety gear (as defined in the regulation) to have tests of that safety gear done every three years, and to send an affidavit to the Branch of the result. The affidavit is completed by the contractor who performs the test, and indicates the types of safety gear present, and whether or not they operated satisfactorily. These tests of the safety gear are only applicable to

devices that are operated by overhead traction, which comprise slightly over one third of the devices in the Province.

Our tests found that 40, or 45%, of applicable elevating devices in our audit sample, had an affidavit on file reporting the results of a test of the safety gear within the last three years. The other 48, or 55%, of our sample did not.

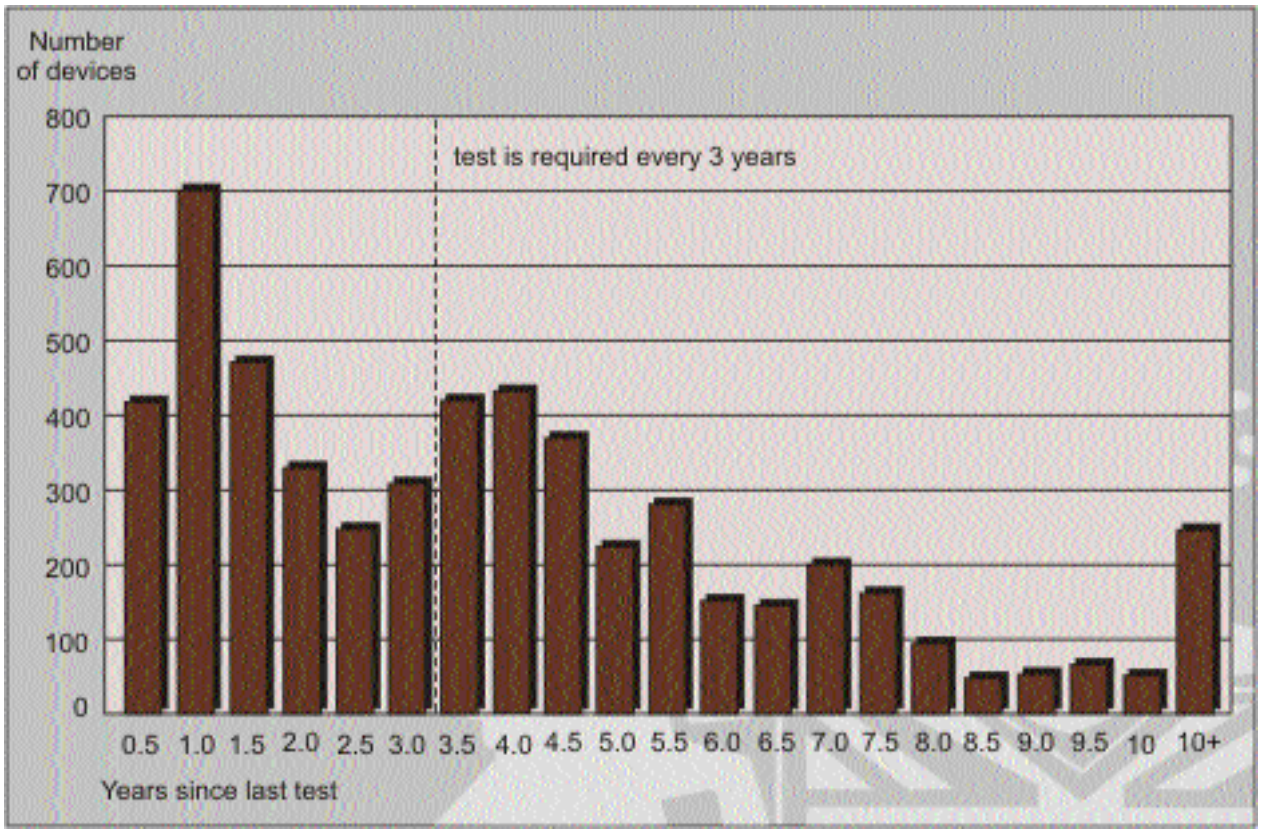
The Branch's own records indicate that 54% of applicable elevating devices (2,969 devices), do not have the required affidavit on file for a safety test conducted within the last three years.

Exhibit 1.4 shows the length of time since the last test of safety gear for applicable elevating devices in the Province, according to the Branch's records.

Officials of the Branch told us they believe that the safety gear tests have been done, but that owners have just been negligent in sending the paperwork to the Branch. During our review, we did come across a few affidavits that had been received some time after the tests were done. We also noted, however, that often the inspector's reports included a direction that a test of the safety gear was overdue and should be done.

Exhibit 1.4

Years Since Last Safety Gear Test



Source: As of July 31, 1994, based on records at the Boiler and Elevator Safety Branch

To investigate further, we wrote to all of the owners of the 48 devices in our sample that had not had a test of the safety gear.

We learned that 13 devices had apparently undergone a test of the safety gear within the last three years, but the affidavit had not been filed at the time of our audit. Eleven other devices had undergone a test of the safety gear since our audit (nine of these had been tested after our confirmation letter was sent out), which meant that the test had been done more than three years after the previous one. Thirteen owners confirmed the last test as being more than three years ago (and there had been no test since the audit), and for nine we got no further information. The remaining two devices that we had thought should have safety gear in fact did not. In summary, we found that while many devices had undergone the required test for which the paperwork came in late, about half had not.

We concluded that the Act is not being satisfactorily complied with in its requirement for tests of the safety gear to be conducted every three years.

We recommend that the Branch follow up with owners on a timely basis to enforce their legal responsibility to have tests of safety gear performed, and to report the results to the Branch.

Licencing of Contractors

Licencing Requirement

Contractors design, construct, install, alter, repair, maintain and test elevating devices. Every contractor must be licenced annually by the Branch. The licence can vary for the type of device the contractor is allowed to work on, and can stipulate whether or not it is for maintenance only.

We identified individuals and companies advertising elevator services in the "Yellow Pages" for five cities in the Province, and looked to see if they were on record at the Branch as licenced contractors. Everyone in the listing was either on record at the Branch or fell into a category that does not require licencing.

We concluded that the Act is being complied with in all significant respects in its requirement that contractors be licenced.

Initial application for licencing

Applicants for a contractor's licence must satisfy the director with respect to company personnel, competence, ability, resources, knowledge of the safety code, training programs and ability to deal with emergencies. Licencing decisions made by the director can be appealed through the Elevating Devices Appeal Board.

For new licences, these requirements are assessed by a panel review process. This consists of an interview, oral examination, inspection of shop facilities, review of pertinent documents, and any other procedures considered necessary.

For the more recent applications, a copy of the oral examiner's notes is on file. For the other aspects of the panel review process, and for all aspects of

earlier applications, there is only the signature of approval by the director to show that the applicant passed the review.

We recommend that the Branch document more thoroughly the assessments carried out in appraising an applicant for a contractor's licence.

Licence renewal

The Act has the same requirement for renewal as for licencing — that is, that the contractor should satisfy the director as to competency, ability and so forth. The procedure for renewals is that the Branch sends out a renewal notice, which the contractor returns with the appropriate fee. We found that there is no formal reassessment of qualifications at the time when the contractor renews the licence. However, at any time during the year a contractor will be reassessed if something comes to the attention of the Branch that suggests a reassessment is necessary, such as complaints or comments from owners, a question arising as a result of an investigation into an accident, or a matter coming to the attention of an inspector.

We believe that it is likely that the contractor may have undergone changes between the initial application and a subsequent renewal. For example, there may have been staff turnover such that the level of training and expertise is not maintained.

We recommend that contractors be required to certify on their licence renewal applications that they still meet the necessary qualifications to be licenced.

Reporting of Accidents

The owner of an elevating device must report to the Branch all accidents that result in injury or death. Fatal accidents must be reported immediately and the device shut down. Injury accidents must be reported within 24 hours. If the safety gear engages, that must also be reported within 24 hours. After being notified of an accident, the Branch and contractor make a site investigation to establish the cause.

We looked at reports of accidents in 1993 and 1994 (up to July). We also reviewed newspaper records from January 1992 to July 1994 about major accidents.

We found that accidents resulting in a serious injury were reported on time, and accidents that were less serious (cuts and scrapes) were often reported late. The exception was accidents on amusement rides where, out of seven accidents that occurred in the three–year period we reviewed, two were reported late: one was two days late, the other eight days late. Both of these accidents resulted in broken bones.

The majority of accidents that are cuts and scrapes occur on escalators. The Branch's experience with these types of accidents is that the equipment is rarely at fault. Rather, the accidents are usually the fault of the users (tripping, for example). Accordingly, for these less serious accidents, they accept monthly summaries of incidents from the owners. Where an accident results in a serious injury, an investigation is carried out by the Branch, as well as by any other appropriate authorities.

Except for the timing of reporting some of the accidents on amusement rides, we concluded that the Act is being complied with, in all significant respects, in its requirements for reporting accidents.

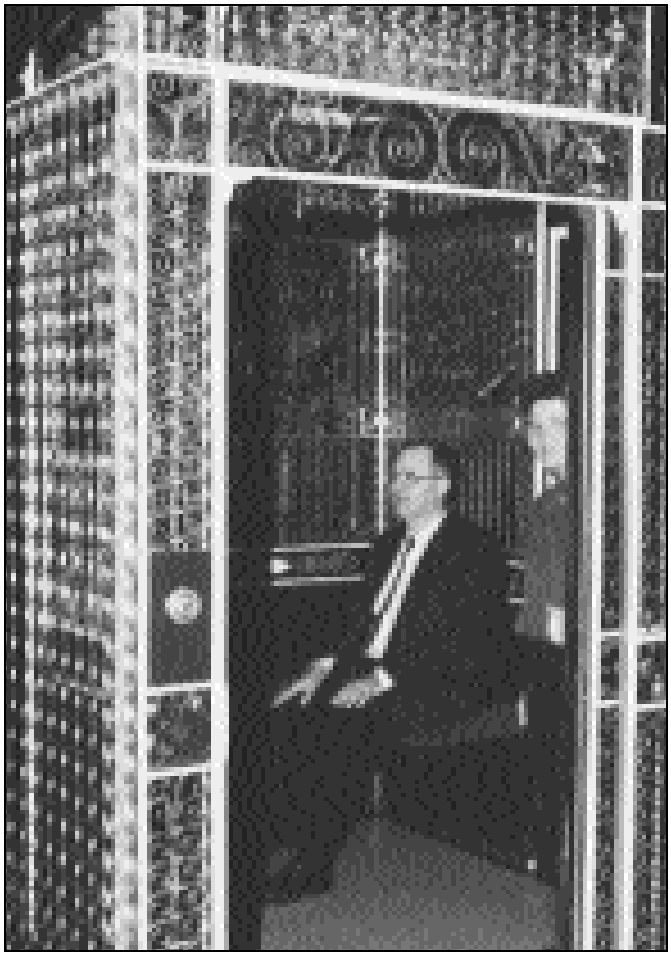
We recommend that the Branch reinforce with owners of amusement rides the legal requirement for reporting accidents within specified time periods.

Other Observations

Risk Assessment Program

According to statistics provided to us by the Branch, in 1980 there were approximately 8,000 elevating devices and 20 inspectors in British Columbia. In July 1994, there were approximately 14,000 devices and 15 inspectors and the average rate of inspection had dropped from once a year to in excess of once every three years. The increasing number of devices adds to the workload in two ways: not only is there an increase in the number of regular inspections that must be done, but each unit also must have an initial acceptance inspection before being put into service, a process that can take up to three or four times longer than a regular inspection.

To better manage the activities of the inspectors, the Branch has developed a computerized risk assessment program — "RAP." This is a database that assigns a score to each device based on various risk factors. The factors are chosen and weighted in such a way that devices which should receive a high priority for inspections, for example because of their type, age, location, or time since the last inspection, will have a higher total RAP score.



One of the oldest operating passenger elevators in British Columbia, in the 1889 Provincial Law Courts building in Victoria, now the home of the Maritime Museum of British Columbia

The database is maintained on a computer in the Branch head office. Each inspector has a portable computer and can communicate via modem with the main computer to download the up–to–date database, and upload information on inspections performed. In addition,

the Branch provides the inspectors with print–outs from RAP showing the devices in their areas with the highest RAP scores, and the devices in their areas that have exceeded the maximum permissible interval between inspections.

The priority for the inspectors is the acceptance tests on new elevating devices, the inspections of construction hoists at least monthly, and the inspections of amusement rides at least annually. Their remaining time is spent performing regular inspections. Once the inspectors have determined where they will be for the acceptance inspections, or construction hoist and amusement ride inspections, they use the RAP score to select devices in the same area or nearby for regular inspections.

We did not assess the weighting assigned to the different factors, but did look at the calculation of the RAP scores for a number of devices. Mathematically, we found the scores to be correct.

One of the more significant factors in a RAP score is the existence of an inspection direction that has not been completed. Depending on how soon it must be completed, a single direction issued by an inspector can add up to 500 points to a RAP score. If the direction should be completed within 10 days, the amount is 500 points; within 11 to 30 days, the amount is 300 points; and within 31 to 90 days, the amount is 50 points. A report can often have five or more directions. We estimated that the average device due for an inspection (almost 3 years having passed since the last one), and with no outstanding directions, will have a score of approximately 1,100 points, or approximately 1,650 points if it is also due for the 3 year safety gear test. Adding in points for an uncompleted direction can significantly increase a RAP score.

We reviewed the RAP scores for 37 devices, concentrating on devices with high scores. The same problem we noted earlier, of owners not informing the Branch when directions arising from inspections have been completed, we found caused a problem with the RAP scores as well. The points relating to a direction are added to the RAP score as soon as the inspection report details are recorded. These points are not removed from the score until the Branch is advised in writing that the direction has been completed, even if there has been a more recent inspection that does not repeat the particular direction. We found a number of such instances.

As a result, we concluded that any score in RAP over approximately 4,000 is likely to be inaccurate, although this would only affect about 100 devices out of the total of 14,000 active units.

We recommend that the Branch develop procedures to ensure that the information in the risk assessment program database, used by the inspectors to priorize their work, is up–to–date and accurate.

Maintenance

There is no requirement in the Act or regulation for the periodic maintenance of an elevating device.

We were told that new devices usually come with a one–year warranty, that includes

maintenance, and that the majority of owners sign maintenance contracts once the warranty has expired. According to the records at the Branch, approximately 3,000 out of the total 14,000 devices do not have a maintenance contract, and so may not be receiving regular maintenance. Maintenance is a factor of the RAP score, although not a significant one.

The Branch would like to see the inclusion of mandatory maintenance in the legislation, and has prepared a draft regulation to this end. If the regulation is adopted, periodic examination and routine maintenance would be required for all devices.

We believe that regular ongoing maintenance is a key factor in giving assurance that elevating devices are safe. Owners or contractors should be required to certify that maintenance is being done.

We recommend that the Act and regulation be amended to require mandatory maintenance for elevating devices, and that confirmation of completed maintenance be reported to the Branch.

Summary of Recommendations

To improve compliance with the Elevating Devices Safety Act *and regulation, the Office of the Auditor General recommends, that:*

- *The Boiler and Elevator Safety Branch develop procedures for following up with owners who have not notified it, as required by the legislation, to ensure that directions have been carried out.*
- *The Branch follow up with owners on a timely basis to enforce their legal responsibility to have tests of safety gear performed, and to report the results to the Branch.*
- *The Branch document more thoroughly the assessments carried out in appraising an applicant for a contractor's licence.*
- *Contractors be required to certify on their licence renewal applications that they still meet the necessary qualifications to be licenced.*
- *The Branch reinforce with owners of amusement rides the legal requirement for reporting accidents within specified time periods.*

To improve operational effectiveness of the Boiler and Elevator Safety Branch, the Office of the Auditor General recommends, that:

- *The Ministry of Municipal Affairs discuss with municipalities the possibility of having them either require a copy of the acceptance inspection certificate before issuing a certificate of occupancy, or inform the Branch when a permit is issued for a building that contains an elevating device.*
- *As part of the acceptance inspection, the Branch require some form of written assurance from the contractor that the device has been constructed in accordance with the Act, regulation and safety codes.*
- *The Branch require an affidavit that the safety tests required by the regulation are up–to–date before it renews the annual certificate to operate.*
- *The Branch update its records to reflect the correct operational status of amusement rides and construction hoists.*
- *The Branch draw up a checklist to document the minimum important procedures that must be performed during an inspection.*
- *The Branch develop procedures to ensure that the information in the risk assessment program database, used by the inspectors to priorize their work, is up–to–date and accurate.*

To provide useful, new legislative authorities relating to elevating devices, the Office of the Auditor General recommends, that:

- *The maximum permissible interval between inspections of elevating devices be specified in the regulation or policies.*
- *The Act and regulation be amended to require mandatory maintenance for elevating devices, and that confirmation of completed maintenance be reported to the Branch.*

Response of the Ministry of Municipal Affairs

The Ministry agrees with the recommendations contained in the Audit Report on compliance with the Elevating Devices Safety Act *and has commenced preparation of an action plan to develop and implement in a timely fashion, the measures necessary to fulfill these recommendations. In particular, the Ministry has assigned top priority to developing procedures to ensure 1) that owners notify the Ministry when they have complied with directions to take corrective action following periodic safety inspections, and 2) that owners fully comply with the statutory requirements respecting regular testing of elevator safety gear and the reporting of the test results. The Ministry notes that, in terms of measurable outcomes related to safety program evaluations, British Columbia enjoys a commendable safety record in the elevator industry.*

We would also note that many of the concerns identified in the report had already come to the Ministry's attention and are currently being addressed within the scope of the Safety Systems Review Project recently initiated by the Ministry's Safety and Standards Department. This comprehensive review of the Ministry's safety inspection programs responds to the increasing difficulty faced by our inspection services in keeping pace with the Province's steady economic and population growth. The aim of this review is to identify the most effective ways to maintain the integrity of our safety systems while responding to contemporary challenges such as constrained resources, increasingly complex technologies and changing client expectations.

Travel Agents Act

Travel Agents Act

The* Travel Agents Act *and related regulation and policy regulate the operation of travel agents in British Columbia, and the Travel Assurance Fund.

Audit Report

Audit Scope

We have made an examination to determine whether the *Travel Agents Act* and related regulation and policy were complied with, in all significant respects, as of August 1994, regarding the initial and ongoing registration of travel agents, the monitoring of their activities, and the operation of the Travel Assurance Fund. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

Audit Opinion

In our opinion, as of August 1994, travel agents were being registered in accordance with the requirements of the Act, in all significant respects, but they were not complying with all the legislative and related requirements to maintain their registration in good standing. The government did not, in our opinion, adequately ensure that the ongoing financial standards and reporting requirements of the Act were being complied with by travel agents. In addition, we found that the Travel Assurance Fund was operating in accordance with the Act, but its required annual report was not being filed.

Introduction

The *Travel Agents Act* and the related *Travel Agents Act Regulations* came into force in 1977. The goal of the legislation is to protect consumers, who have prepaid for travel services, from monetary loss.

Consumers in British Columbia who want to make travel arrangements involving airline or bus transportation and hotel accommodation may purchase these services directly from the suppliers or through travel agents. There are two types of travel agents operating in the Province. Retail agents resell to the public those travel services supplied by others, such as airlines, cruise ship companies and travel wholesalers. Wholesaler agents put together their own travel packages, including transportation and accommodation, and offer these packages to the public or to retail travel agents.

The travel agent industry is a business that often does not require a large investment of funds and provides a product or service that is usually prepaid by consumers. Currently, there are more than 1,000 travel offices in British Columbia. Many of these are owned and operated by small business operators. To reduce the risk of monetary loss to the consumer, the Act requires that all travel agents selling retail or wholesale travel services to the public register in accordance with the requirements of the Act.

The Act and regulation provide two means of protecting consumers. First, they establish requirements for the operation of travel agents in British Columbia; second, they establish the Travel Assurance Fund. The Office of the Registrar of Travel Services, a branch of the Ministry of Housing, Recreation and Consumer Services, has been established to administer the legislation. The Branch only regulates travel agents. The Branch has a staff of four people to perform these duties. The person who is the Registrar also has other responsibilities in the ministry, unconnected with the *Travel Agents Act*.

The Branch is responsible for ensuring that all travel agents in the Province selling wholesale or retail travel services to the public are registered in accordance with the requirements prescribed by the Act and the regulation. This responsibility includes monitoring the financial soundness of registered travel businesses and, where necessary, provides the discretionary authority to cancel, suspend or close those businesses found not complying with the Act and regulation.

The Travel Assurance Fund is made up of monies collected from the travel industry. The fund is used to compensate the consumer or another travel agent in the event of a travel business failure, but only if the eligible consumer or travel agent purchased the travel services through a registered travel agent. The fund is administered by the Registrar of Travel Services and the Travel Assurance Board, whose members are appointed by the Lieutenant Governor in Council.

A public carrier, for example an airline, passenger rail or bus company, can choose to be

exempted from the Act provided it agrees to: waive claims against the fund (for example, should there be a business failure by a registered agent who had sold the services of that carrier); contribute to the fund, though to a lesser extent than a registered agent; honour all tickets issued by or on behalf of itself and interconnecting carriers; and advise the Branch when it removes tickets from any registered agent. Consequently, consumers who purchase travel services directly from an exempt public carrier are not covered by the Travel Assurance Fund. All of the public carriers operating in British Columbia at the time of our audit had chosen to be exempted from the Act.

The Act also exempts specific types of travel businesses, as detailed in Exhibit 2.1.

Audit Scope

Our audit was conducted to determine whether the government has complied with, and ensured travel agents have complied with, in all significant respects, the following main requirements of the *Travel Agents Act* and related regulation and policy, as of August 1994:

- the applicant must be 19 years of age, and a British Columbia resident;
- the business must operate from a commercial location;
- the applicant should have a positive net worth position and a positive working capital position at the time of application, and maintain this position while in operation;
- applicants for registration shall be assessed on specific financial and ethical considerations;

Exhibit 2.1

Exempt from the Act

- an operator of one–day sightseeing tours whose principal business is providing sightseeing tours;
- a person providing guide services only where no other travel services are sold;
- a person providing sightseeing attractions where no other travel services are sold;
- a public carrier, while providing one-day tours;
- a teacher or instructor who arranges travel services for students of his or her school without direct or indirect gain or profit;
- an operator of a motel, hotel, resort or other accommodation who offers incidental local travel services purchased from another person; and
- the BC Ferry Corporation when it is selling interconnecting, scheduled travel transportation.

Source: The *Travel Agents Act* Regulations

- applicants shall have never been convicted of an offence under the *Immigration Act* (Canada) or contravened the *Travel Agents Act* or another statute of the Province;
- applicants shall have sufficient experience in the business, or employ staff with sufficient experience;
- the applicant must provide a statutory declaration to the Registrar that all information provided on the application is true;
- travel agents shall keep in trust all money received from purchasers of travel services until the money is transferred to the provider of those services;
- travel agents shall pay prescribed annual fees by specified dates;
- travel agents shall make prescribed contributions to the Travel Assurance Fund;
- travel agents shall prominently display their registration certificate;
- travel services in the Province shall only be offered by those businesses that are registered, unless exempted under the Act;
- the Branch shall maintain a register of all registered travel agents;
- every business or trade name used by an agent shall be registered;
- travel agents shall maintain prescribed business records and file annual financial statements with the Branch certified as correct by the owners or directors;
- the Branch shall maintain records for the Travel Assurance Fund showing revenue, amounts receivable and received and amounts paid as claims or other expenditures;
- travel agents shall obtain the written consent of the Branch before they transfer their registration to another party; and
- the Travel Assurance Board shall file an annual report on the operation of the fund.

We reviewed the records at the Office of the Registrar of Travel Services, a branch of the Ministry of Housing, Recreation and Consumer Services, for a sample of 157 registrations, owned by 146 agents, to determine whether their registrations were in compliance with the Act. We visited 81 agents in Vancouver, the Lower Mainland and on Vancouver Island to see if they were registered and displaying their registration certificates.

We did not carry out procedures to verify the registrants' qualifications related to past conduct, good character, and compliance with other laws. For these and other qualifications we relied on the information available at the Branch. In addition, we did not audit the sections of the Act that establish the Travel Assurance Board or the sections that deal with the board's practices and procedures, except with regard to the operation of the Travel Assurance Fund and the requirement for tabling an annual report on the operation of the fund.

Overall Observations

Overall, we found that:

- the requirements for the initial registration of travel agents were complied with in all significant respects, except that:
  - although the Branch did obtain a declaration from the applicant that the information on the application form is true, it was not sworn, as required by legislation;
  - in some cases, agents were allowed to operate their business in the name and registration of the current registrant during a change or transfer of ownership before they had been newly registered;
- the licence certificates were not prominently displayed in half of the offices we visited, and cancelled licence certificates were not returned;
- the majority of travel businesses operating in the Province, and not exempt from the Act, were registered;
- the requirements for maintaining registration in good standing for travel agents were complied with in all significant respects, except that:
  - almost 30% of financial statements were not submitted in a timely fashion, and 50% were not certified as correct by the owners or directors;
  - the net worth and working capital position were not maintained by about 30% of travel agents; and
  - 33% of the annual licence fees were paid late;
- the required contributions were being made to the Travel Assurance Fund, payments from the fund were properly made, and the necessary records were kept;
- all agents had opened trust accounts, although since we did not have access to the private business records of the agents, we were unable to determine if the trust accounts were being used for the deposit of payments from consumers and were being operated in a proper manner;
- transfers of ownership or control were properly handled;
- the monitoring program of field visits initiated by the Branch was inadequate;
- the Branch has imposed fees for late filing, without the authority of the Act or other legislation, and these fees were sometimes waived without the authority of the *Financial Administration Act*; and
- the Travel Assurance Board has not provided to the minister, for tabling, an annual report on the operations of the fund since 1988.

Audit Findings

Application for Registration of Travel Agents

At the time a travel agent applies for registration, the Branch verifies that the agent has complied with the requirements of the Act.

The applicant must be 19 years of age or older, a resident of British Columbia, and proposing to operate at a commercial location. A separate application must be made for each location. The applicant must meet certain financial requirements. The Branch must consider if the applicant possesses relevant experience, is of good character, and has never been convicted of an offence under the *Immigration Act* (Canada) or contravened the *Travel Agents Act* or another statute of the Province. The applicant must have a trust account at a financial institution for the deposit of consumer payments. The application must be accompanied by the prescribed fee and the initial application to the Travel Assurance Fund.

The Branch can refuse to grant registration where it appears that these criteria have not been met, or where it appears that registration would not be in the public interest.

The Branch may also place restrictions on the applicant. For example, the applicant's business may be restricted to selling only one type of travel package, or, if the Branch considers that the applicant's experience is insufficient, the Branch may require that an experienced resident manager be employed before a registration is granted.

Age, residency and commercial location

We found that every applicant had provided the appropriate information about age, residency and commercial location, and had met the requirements of the Act.

Financial requirements

The legislation and the related policy require that applicants have a positive net worth position and a positive working capital position, supported by current financial statements; and that those who are a corporation have a minimum net worth position of at least $15,000.

In addition to this, the Branch has also required, since 1987, that applicants for a retail registration submit and maintain an irrevocable letter of credit for a minimum of $15,000, plus $5,000 for each branch location, and applicants for a wholesale registration submit and maintain an irrevocable letter of credit for an amount determined by the particular circumstances.

Whether an applicant's net worth and working capital requirements have been met is determined based on financial statements submitted by the applicant. These financial statements can be prepared by the applicant or by public accountants. In some cases, pro forma financial statements appeared to be considered acceptable.

"Net worth position" is defined by regulation as the dollar difference between the value of total assets and the value of total liabilities which have been ascertained in accordance with ordinarily accepted accounting standards and principles.

"Working capital position" is defined by regulation as the dollar difference between the value of current assets and the value of current liabilities which have been ascertained in accordance with ordinarily accepted accounting standards and principles.

We found in our audit that an appropriate letter of credit was on file for all of the applications made since 1987, when the requirement for the letter of credit was introduced.

We also found in 152 registrations out of the 157 in our audit sample that the net worth and working capital criteria had been met. In the remaining five, registrations were granted after the agents, at the Branch's request, had provided undertakings to increase equity, such as board resolutions or, in one case, a fax from a notary public stating that such a resolution was being prepared.

Experience, character and personal history

Applicants are asked to assess their experience, knowledge and past conduct in a series of yes/no questions. These questions include matters relating to previous offences, bankruptcy, money matter litigation, and work history. The personal history forms are required to be completed by each owner, partner or officer in an agency, and three directors of a corporation, except where the total number of directors is fewer. For an extra–provincial corporation, the form must be completed by not fewer than three directors who are ordinarily resident in the Province. In addition, any resident manager must also complete the form.

The applicant must have at least two years' travel industry experience, obtained in the previous five years.

Current practice of the Travel Services Branch is to accept the information as reported in the application form and personal history forms. Generally no verification of past conduct is undertaken. However, the Branch performs employment reference checks to verify work experience. Applicants with insufficient experience are required to obtain the services of an experienced resident manager.

For all of the files in our audit sample we found that the required forms had been completed and filed, and employment reference checks performed.

Trust account

Branch policy requires travel agents to maintain separate trust bank accounts. Prior to September 1993, the existence of the trust bank account was confirmed over the phone, or by correspondence where necessary, with the related financial institution. Currently, an applicant is required to submit with the application a list of the trust and general accounts opened by the applicant. The list must be signed by an authorized signing officer of the financial institution where the accounts are maintained.

We found that all the appropriate documents were on file to show that all the applicants in our sample had opened trust bank accounts.

Statutory declaration

The application form prescribed by the regulation includes a statutory declaration, to be completed by the applicant and sworn before a commissioner for taking affidavits, that all the

information provided on the application is true.

We found that while the form being used by the Branch does include a certification by the applicant that all the information given on the application is true and correct, it does not make provision for it to be sworn before a commissioner for taking affidavits.

Fee and initial contribution to the Travel Assurance Fund

The application must be accompanied by a fee of $275, as well as an initial contribution to the Travel Assurance Fund of $300 for each registered office.

We found that all of the fees and contributions necessary for the applications we looked at had been paid.

Registration process

The registration process normally takes four to five weeks to complete. Where documentation is incomplete, however, the process may take longer. The Branch informed us that an applicant who is buying an existing business may be allowed to operate their business in the name and registration of the current registrant during a change or transfer of ownership before they have been newly registered.

Conclusion

We concluded that, except for the alteration of the prescribed form to remove the statutory declaration, the Act and regulation were being complied with, for the initial registration, in all significant respects.

We recommend that the Branch either use the form of application prescribed by regulation, or obtain legislative approval for the form in current use.

We recommend that, in cases where a travel agent has not provided an undertaking to meet the net worth and working capital requirements, registration be withheld.

Licence Certificate Issued on Registration

Once a travel agent's office has been registered, a licence certificate is issued. The certificate lists the business names of each travel agent registered, address, registration number, and restrictions, if any. It also shows the effective date that an agent is registered, but no expiry date.

The certificates are prepared by the Branch. We found that the required information was being included, and that the certificates were being issued to the agents.

Travel agents are required by regulation to display the certificates prominently so that members of the public can see them. To verify compliance with this requirement, we visited 81 offices in Vancouver, the Lower Mainland, and on Vancouver Island. We found that 50% of the travel offices we visited did not comply with this requirement.

The certificate is also required by regulation to be returned when an office is closed or if the registration is cancelled for some other reason. We reviewed the files of 30 offices that had been closed, and found only 1 returned certificate.

We concluded that the requirements of the Act and regulation for the display and return of certificates have not been complied with.

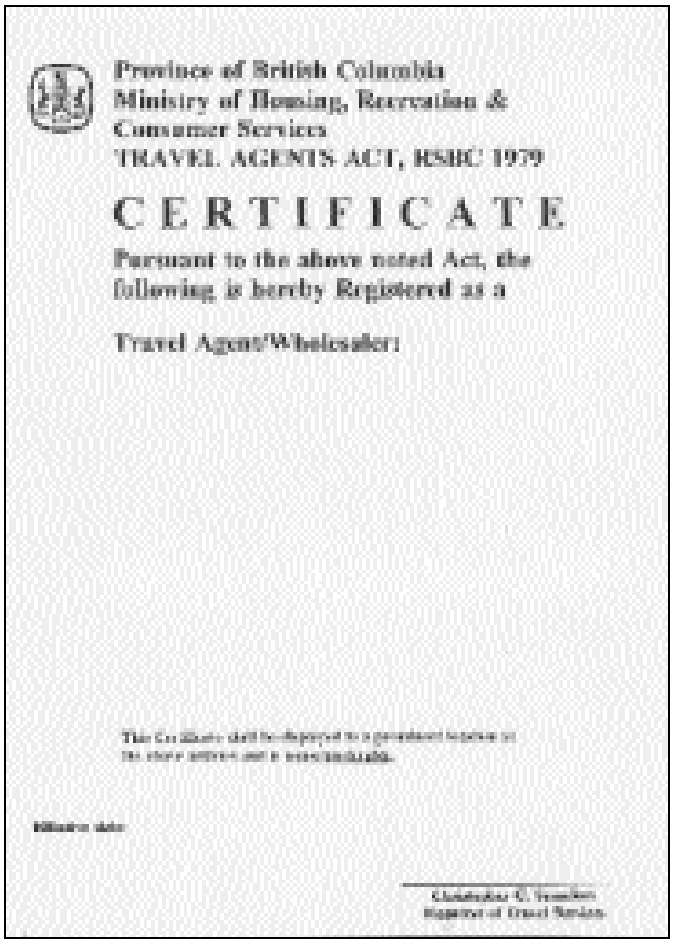
We recommend that the Branch remind travel agents of the legislative requirement to display their registration certificate, and to return the certificate when the registration is cancelled.

We also believe that it would be useful to include on the certificate a reference to the Travel Assurance Fund, as well as an expiry date.

Monitoring of Non-registered Businesses

As previously stated, only registered travel agents, apart from those specifically exempted, can offer travel services. They must conduct business under the registered name, and may have more than one trade or business name, as long as each one is registered. The Act also requires each office where a travel business is carried on, or is intended to be carried on, to be registered separately. Registrations must be renewed every year. The Branch maintains a list of all travel businesses ever registered, indicating whether they are currently in business or have closed.

The Branch currently maintains a number of informal information exchanges with various industry organizations. Although the Branch does not actively monitor the market to identify travel agents operating without being properly registered,



Province of British Columbia
Ministry of Housing, Recreation & Consumer Services
TRAVEL AGENTS ACT, RSBC 1979

CERTIFICATE

Pursuant to the above noted Act, the following is hereby Registered as a

Travel Agent/Wholesaler:

Licence certificate

it does receive information on problems that have come to the attention of other industry members, government bodies such as the Motor Carrier Commission which licences tour bus operators, business licencing departments of major municipal governments, and consumer interest groups such as the Better Business Bureau.

Information from these third parties has aided the Branch in identifying some unlicenced operators. For example, about 20 cease and desist orders were issued during the first eight months of 1994 as a result of information received from these sources.

However, several months may elapse before an unlicenced travel agent is brought to the attention of the Branch, and some are likely never detected.

To assess whether or not all travel agents were registered, we reviewed a number of yellow page listings, business directories, and advertising in newspapers. In total we identified over 900 travel offices, which we then compared to the register.

Only six travel businesses did not match up, one of which may have been operating for several years. These six exceptions were brought to the attention of the Branch which has taken corrective action, including issuing cease and desist orders. We also found six registered travel agents which were operating under non–registered business names.

Apart from these exceptions, we concluded that all travel businesses operating in the Province are registered in accordance with the Act.

We recommend that the Branch periodically monitor advertisements, business directories, and the like, and conduct any other appropriate procedures to ensure that all travel businesses are registered if they are not of a type exempted by the Act.

We recommend that the Branch consider establishing formal arrangements to exchange information with other government and industry agents such as municipal business licencing departments.

We understand that motor dealers in British Columbia are required to include their registration number on all advertising in the Province. The Province of Ontario requires the same of all registered travel agents in that Province. We believe that such a procedure could be helpful in monitoring the travel business in British Columbia.

Maintaining Registrations in Good Standing

In order to maintain their registration in good standing, the Act and regulation require the registered travel agents to:

- submit financial statements within 90 days of their fiscal year end;
- maintain the required net worth and working capital requirements;
- process payments received from consumers through the trust accounts;
- pay an annual licence fee; and
- make the appropriate contributions to the Travel Assurance Fund.

Timely submission of financial statements

Travel agents are required to file their financial statements annually, within 90 days of their fiscal year end.

Out of the 146 agents in our audit sample, 100 had done so, 40 had filed late, varying between two and six months late, and, at the time of our audit, 6 were overdue. Three of the six were more than two years overdue, yet these agents were still being permitted to operate. The 40 that had filed late

included 4 who had been one year overdue for the prior year.

The financial statements can be prepared by the agent or by professional accountants. They must also be certified as correct by owners or directors. Although the Branch has the power to request agents to submit audited financial statements, it has not exercised this option, although some audited financial statements are, nevertheless, submitted on a voluntary basis.

We found that only 70 of the 140 statements that had been filed had been certified as correct by the owners or directors.

Ongoing net worth and working capital requirements

Travel agents are required to maintain a positive net worth and working capital position and, if a corporation, a net worth of at least $15,000. This is assessed on an ongoing basis each time the financial statements are filed.

Of the 140 statements in our audit sample, we found that 33 did not meet the net worth requirement, 8 did not meet the positive working capital requirement, and 7 met neither requirement. To determine this we used the definitions of net worth and working capital set out in the regulation. This finding is consistent with the Branch's own estimation of the financial status of all the registered travel agents.

The Branch informed us that suspending or closing an agent would expose the consumer or the Travel Assurance Fund to immediate monetary loss. As a result, we found the Branch tended not to suspend or cancel a registration, but instead to extend deadlines and work with the agent.

For example, in the situations where the net worth or positive working capital requirement was not met, we found that the Branch would:

- recommend that the agent consult business advisors and inform the Branch of the results;
- suggest that the agent convert a shareholder loan to equity, or inject new capital;
- suggest that the agent obtain an increase in the amount of a letter of credit; or
- require from the agent updated financial information, perhaps on an ongoing basis.

These procedures are designed to allow a business to continue on a temporary basis while the Branch decides the optimal time to suspend or close a business that cannot improve its financial position.

The Branch bases its decision on an analysis of the financial statements and on financial information about registered agents received from trade creditors, airlines, trade organizations, and other members of the industry. Registered agents are required by regulation to notify the Branch when they cease to trade with another registered agent because of that agent's failure to honour a cheque or other financial commitment. However, we found that there is no documented guidance on the appropriate action to be taken by Branch staff.

Processing payments received through trust accounts

The Act states that money received from consumers is deemed to be held in trust for the person who paid it. As a result, the Branch's policy requires travel agents to maintain separate trust bank accounts, and to deposit in them that money received from consumers. The amount of any fee or commission cannot be taken from the trust account until the required amount has been paid over to the provider of the travel services. The Branch has issued a trade bulletin describing trust accounting procedures.

We found that the Branch does not have a program of field audits to actively monitor compliance with this policy. Since we did not have access to the private business records of the agents, we were unable to determine for ourselves if the trust accounts were being operated in a proper fashion.

Annual licence fee

The regulation requires all travel agents to pay an annual licence fee of $275 for each office in the Province. The renewal date can be at any time throughout the year, but it is Branch policy that all licences expire on March 31 and payment of the annual licence fee is due April 9, 1994.

We found that all the agents in our sample had paid the annual fee, but the majority had done so after the licence had expired. We identified 52 late payments of which the majority were made before April 30, but 19 were late by one or more months.

Contributions to the Travel Assurance Fund.

Registered agents are required to make semi–annual contributions to the Travel Assurance Fund, within 40 days of February 28 and August 31 as prescribed by regulation. These contributions must be made for a minimum of three years after the agent is initially registered. After that, if the fund is at a balance of $1,000,000 or more, the minister may declare a contribution holiday. That holiday has been in effect since April 1994.

An agent's contribution to the fund is equal to 5/100 of 1% of gross revenue received for non-scheduled travel transportation services. Scheduled travel transportation means travel transportation supplied on a regular basis at fixed times and for which advance booking is not required. Contributions are to be reported on a prescribed form and are self–assessed.

The Branch periodically reviews the contribution forms to consider the reasonableness of the amount and to check the accuracy of the calculation.

Forty–five agents in our audit sample were not entitled to the contribution holiday and must therefore make a contribution. We reviewed the February 28, 1994 fund contributions made by these travel agents and found that most contributions were made before the due date of April 9, 1994. Two payments were still outstanding at the time of our audit. We have been advised that they were subsequently collected.

Conclusion

We concluded that the Act and related regulation and policy, in their requirements for ensuring that travel agents are in good standing, are not being complied with. Many financial statements are not being submitted within the time allowed by legislation and are not properly certified; at any point in time it appears that almost 30% of agents are not in compliance with the net worth and positive working capital requirements; and most of the annual licence fees are being paid late. Because we did not have access to the private business records of the agents, we were unable to determine whether or not the trust accounts are being properly used. Regarding contributions to the Travel Assurance Fund, the Act is being complied with, although the majority of agents are not required to contribute at this time.

We recommend that the Branch take steps to ensure compliance with the following requirements; specifically, that travel agents:

- *file financial statements within 90 days;*
- *have financial statements certified by the owners or directors;*
- *maintain the net worth and working capital required by the Branch; and*
- *pay the annual licence fee on time.*

We recommend that the Branch consider what steps it might take to determine whether travel agents are operating their trust accounts as required and, if necessary, what steps it might take to ensure compliance.

The Travel Assurance Fund

The Travel Assurance Fund, established under the Act, is the final safeguard for the consumers. Every registered travel agent doing business in British Columbia is required to contribute to the fund. The Fund is used to compensate an eligible consumer or registered agent who has lost money from cancelled services purchased through a registered agent. Money, or direct economic loss, is defined as reasonable out–of–pocket expenses incurred for such items as transportation, accommodation, meals, sightseeing, and events, but is limited to amounts actually paid by the client. A client is defined by regulation as a British Columbia resident who has contracted in the Province to purchase travel services through or from a registered agent. Non–residents are covered for purchases through or from registered agents for travel services that will take place wholly in British Columbia. A British Columbia resident who purchases travel services through an agent located in another Province or country is not covered by the Travel Assurance Fund.

We audited 30 payments from the fund made between January and August 1994. These totaled about $27,000, or about 75% of the payments made during that time. We found that all of the payments were properly made in compliance with the Act.

As already noted above, travel agents are required to make an initial contribution to the fund on registration, and semi–annual contributions for at least three years after that. If the balance in the

fund reaches $1,000,000 or more, further contributions after the first three years may be waived. The fund reached $1,000,000 in March 1994, and most agents now are enjoying a contribution holiday.

We determined that agents were making the required contributions to the fund, and that appropriate records are being maintained.

Although we did not attempt to assess the adequacy of the fund, we did review the trend of contributions to and payments from the fund since it was established in 1978. This is shown in Exhibit 2.2.

History suggests there is a cyclical trend of contribution surpluses and deficits that will likely continue. The legislation provides means of collecting additional contributions from travel agents, and also provides for obtaining loans from the provincial Consolidated Revenue Fund if it is necessary to do so until contributions can cover any shortfall. This has happened on occasion. The $1,000,000 level for the fund was established in 1993.

Change of Ownership or Control

Ownership or control of travel agents changes from time to time. With the written consent of the Branch, the registration may be transferred as well. In these cases, the transferee does not need to pay an initial registration fee or make an initial contribution to the fund.

The Act defines “transfer” to include a change of proprietor, a change in the number of partners in the case of partnership, or a material change in the beneficial ownership of the shares of a corporation.

We found that where transfers had occurred, written consent of the Branch had been given.

Monitoring for Compliance

The Act and regulation allow the Branch to inspect an agent to ensure compliance with the legislation, and to appoint an investigator when it is believed that a person has contravened, or is about to contravene, the legislation.

Registered agents are seldom inspected for compliance. We noted that although the Branch has introduced an inspection program, it does not apply in the Greater Vancouver and Greater Victoria areas, which is where most of the travel offices are concentrated. This program includes steps to check that agents are operating out of commercial premises, licences are displayed, the names used on signs and advertisements are registered, financial records are kept, and bank accounts are kept for general and trust funds. However, detailed inspections of financial records, to verify the filings made by the agents and operations of the trust accounts, are normally not performed during these inspections.

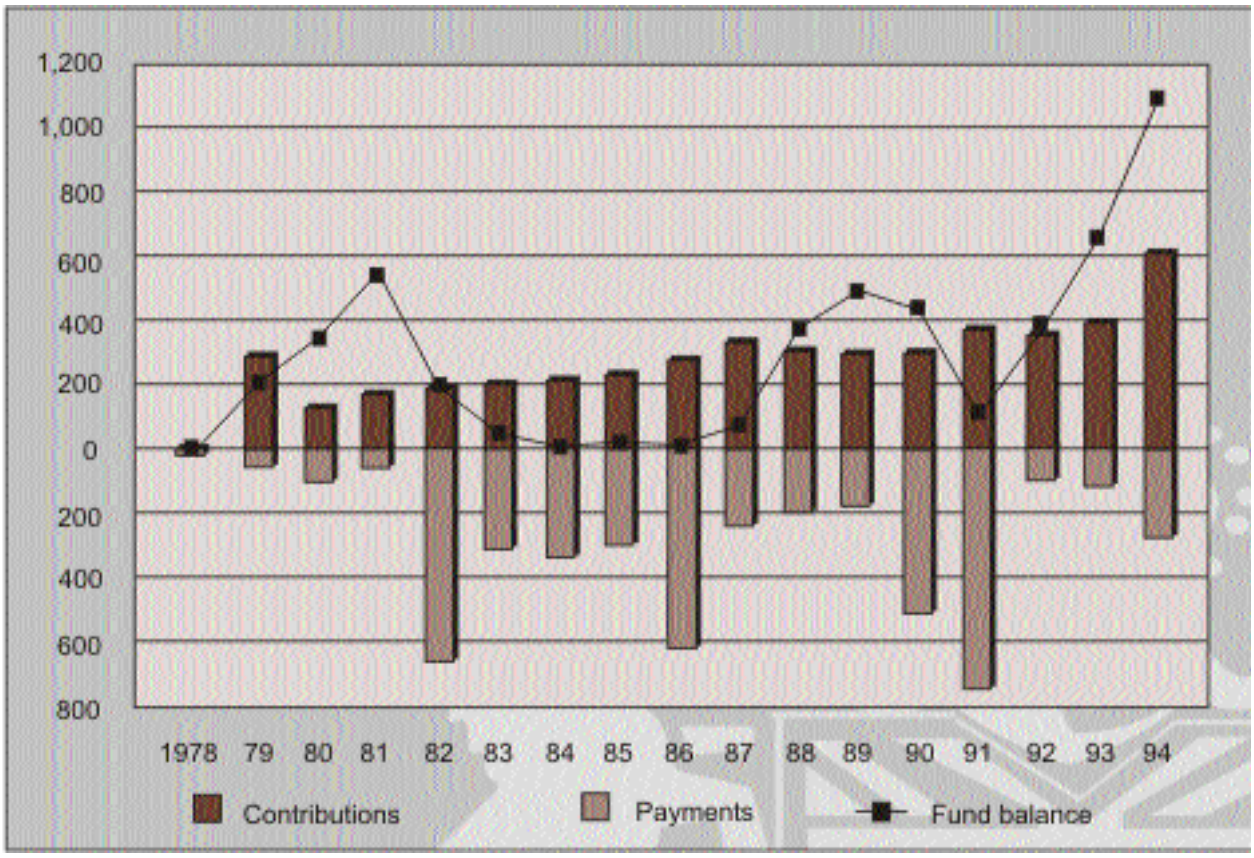
Twenty–one inspections were performed during fiscal 1993/94, but only two inspections were performed between April 1994 and November 1994 because of staff shortages at the Branch.

We recommend that the inspection program be expanded to

Exhibit 2.2

Contributions To, Payments From, and the Balance of the Travel Assurance Fund

Fiscal years ending March 31 ($ Thousands)



Source: Office of the Registrar of Travel Services

include the Greater Victoria and Greater Vancouver areas, and that it include a review of the operations of the trust accounts.

Administration Charges

To encourage prompt payment of fees, contributions to the fund, and filing of financial statements, it is Branch policy that agents be charged administration fees for late submission of these items. This policy has been communicated to registered agents in a bulletin. These fees are of the order of $50 to $100 for each month an item is overdue, but no interest is charged on overdue amounts. The Act itself contains no provisions for the levying of these fees.

We question the validity of these fees. The *Financial Administration Act* not only forbids the charging of fees without proper authority, but it requires the charging of interest at a prescribed rate on amounts owing to the government. On both counts, the

Branch's administrative fees seem to be contrary to legislation.

We also found that these fees are recorded only when they are received, rather than when they are receivable. This is not in accordance with the Financial Administration Operating Policy Manual of the government, which requires that all amounts due to the government be promptly recorded in the accounts of the ministry.

As well, we noted that in some instances the Branch would sometimes waive these fees. This again is in contravention of the *Financial Administration Act*. The authority to waive amounts is limited by Treasury Board Directive to certain authorized persons and does not include anyone at the Branch.

We recommend that the Travel Agents Act be amended to provide the Branch the legal authority to levy fines or administration charges or, alternatively, that the Branch obtain the necessary authority, as required by the Financial Administration Act*, to levy these fines and charges.*

We recommend that interest be charged on amounts owing to the Province in accordance with the rate prescribed under the Financial Administration Act.

We recommend that the Branch comply with the Financial Administration Act *when waiving amounts owing to the Province.*

Annual Reports

The Act requires the Travel Assurance Board to file an annual report with the minister who shall table it in the Legislative Assembly within 90 days of the end of the fiscal year for which the report is made, or within 15 days of the opening of the next session if the assembly is not sitting at that time. The report should include information on the total amount of all receipts in the fund, the amount of all payments by the fund, a statement of all claims, and a statement of amounts owing by registered agents to the fund.

We found that the last report produced was for the fiscal year ended March 31, 1988. No report has been produced since then. Although mention is made in the annual report of the ministry responsible for the Travel Services Branch — currently the Ministry of Housing, Recreation and Consumer Services — this does not include any of the required information.

We recommend that the Travel Assurance Board bring its overdue filing of annual reports up to date, in accordance with the requirements of the Act.

Summary of Recommendations

The Office of the Auditor General recommends, that:

- *The Branch either use the form of application prescribed by regulation, or obtain legislative approval for the form in current use.*
- *In cases where a travel agent has not provided an undertaking to meet the net worth and working capital requirements, registration be withheld.*
- *The Branch remind travel agents of the legislative requirement to display their registration certificate, and to return the certificate when the registration is cancelled.*
- *The Branch periodically monitor advertisements, business directories, and the like, and conduct any other appropriate procedures to ensure that all travel businesses are registered if they are not of a type exempted by the Act.*
- *The Branch consider establishing formal arrangements to exchange information with other government and industry agents such as municipal business licencing departments.*
- *The Branch take steps to ensure compliance with the following requirements; specifically, that travel agents:*
  - *file financial statements within 90 days;*
  - *have financial statements certified by the owners or directors;*
  - *maintain the net worth and working capital required by the Branch; and*
  - *pay the annual licence fee on time.*
- *The Branch consider what steps it might take to determine whether travel agents are operating their trust accounts as required and, if necessary, what steps it might take to ensure compliance.*
- *The inspection program be expanded to include the Greater Victoria and Greater Vancouver areas, and that it include a review of the operations of the trust accounts.*
- *The* Travel Agents Act *be amended to provide the Branch the legal authority to levy fines or administration charges or, alternatively, that the Branch obtain the necessary authority, as required by the* Financial Administration Act, *to levy these fines and charges.*
- *Interest be charged on amounts owing to the Province in accordance with the rate prescribed under the* Financial Administration Act.
- *The Branch comply with the* Financial Administration Act *when waiving amounts owing to the Province.*
- *The Travel Assurance Board bring its overdue filing of annual reports up to date, in accordance with the requirements of the Act.*

Response of the Ministry of Housing, Recreation and Consumer Services

This Ministry appreciates the opportunity to respond to the findings of the Auditor General with respect to the recent compliance audit under the Travel Agents Act, *regulation and related policy.*

Our response to your findings and recommendations follows:

Application Form

As the audit found that the application form currently being used by the Branch is not that required by statute they recommended that the Branch either utilize the form prescribed by statute or obtain legislative approval for the form currently in use.

A request for an Order in Council (OIC) change to the regulation has been made as the application form and other forms prescribed and exhibited in statute do not meet current marketplace requirements.

Working Capital and Net Worth Requirements

Your Report recommends that the Branch not register or renew applications where there is no undertaking to meet the net worth and working capital requirements as well as ensuring that this requirement is maintained by registrants.

We concur with your recommendation.

Registration Certificate

We concur with your recommendation. The Inspection program will ensure compliance with respect to display of certificate.

Monitoring for Non–registered Businesses

We concur. This activity will be intensified, although the travel industry itself is quick to help us identify non–registrants.

Many formal arrangements are currently maintained for exchange of information and new ones are being constantly established.

Maintaining Registration in Good Standing

You recommend that registrants be reminded of their requirement to comply with statute requirements, specifically:

- *file financial statements within 90 days*
- *have financial statements certified by owners or directors*
- *maintain the net worth and working capital required by the Branch*
- *pay the annual license fee on time.*

We concur with your recommendations and the travel industry has been recently advised of legislative requirements.

Operation of Trust Accounts

We concur with your recommendation. The Ministry is studying the development of a process to ensure the correct operation of trust accounts by registrants.

Monitoring for Compliance — Inspection Program

We concur with this recommendation and the Inspection program has recently been expanded to comply with the recommendation.

Administration Charges

The Ministry believes that the authority to levy and collect administration charges is given under Section 4(4) of the Act which provides to the Registrar of Travel Services the discretionary authority where it says: "the registrar may register or renew registration on the terms, conditions or restrictions he considers necessary...".

Annual Reports of the Travel Assurance Board

The Ministry believes that it has complied with the requirements as the reports of the Travel Assurance Board have been included as part of the consolidated Annual Report of the Ministry. However, a consolidated report for the deficient time period will be prepared and tabled. Future Ministry Annual reports will contain an expanded section on the Travel Assurance Board and the Travel Assurance Fund as required.

Financial Administration Act: Guarantees and Indemnities

Financial Administration Act: *Guarantees and Indemnities*

The* Financial Administration Act *and related regulation and policies enable the Province to provide guarantees and indemnities to borrowers and contractors, subject to certain authorizations and other conditions.

Audit Report

Audit Scope

We have made an examination to determine whether sections 56 to 58 of the *Financial Administration Act*, the *Guarantees and Indemnities Regulation*, and the related Treasury Board policies which provide for the approval, control, and reporting of guarantees and indemnities, were complied with, in all significant respects, between April 1, 1991 and March 31, 1994. Our examination was made in accordance with generally accepted auditing standards and accordingly included such tests and other procedures as we considered necessary in the circumstances.

Our examination identified a risk that indemnities may be included in contracts or agreements without meeting the approval requirements of the *Financial Administration Act* and its related regulation. Because we considered it impracticable to identify a representative sample of all agreements which might include indemnity clauses, our audit testing was limited to indemnities reported by the Risk Management Branch, ministries and government corporations.

Audit Opinion – Guarantees

In our opinion, the legislative requirements for the approval, control and reporting of guarantees were being adequately complied with, in all significant respects, between April 1991 and March 1994. However, the more detailed Treasury Board policy requirements relating to the approval of guarantees were not being adequately complied with during this period.

Audit Opinion – Indemnities

In our opinion, the legislative requirements for the approval, control and reporting of indemnities were not being adequately complied with between April 1991 and March 1994.

Introduction

The *Financial Administration Act*, the *Guarantees and Indemnities Regulation*, and the related Treasury Board policy as specified in the government's Financial Administration Operating Policy Manual govern the approval, control and reporting of most guarantees and indemnities given by ministries and government organizations. Although there are 27 other statutes that also contain provisions for giving guarantees, in general these powers are not exercised.

The Act states that guarantees and indemnities may only be given in compliance with the regulation. The regulation specifies the required approvals, and Treasury Board policy details the procedures which must be followed in order to adequately approve, control and report guarantees and indemnities.

Guarantees

Commercial loan guarantees, the subject of this audit, are given by government to provide security for businesses that would otherwise be unable to obtain commercial loans from financial institutions. In any guarantee agreement, there are three parties: the financial institution, organization or individual who lends the funds; the borrower; and the guarantor, in this case the Province of BC, who promises to repay the loan to the lender if the borrower is unable to do so.

The practice of giving guarantees, instead of loans or grants, reduces the amount the government disburses to support industry, small business and agriculture in the Province, because money is spent only if a business defaults on its guaranteed loan.

During the three–year period of our audit, April 1, 1991 to March 31, 1994, the government approved $86 million in loan guarantees to commercial enterprises. It did so through a variety of programs:

- to small businesses, under the Small Business Assistance Program, the Business Expansion Program and the Job Protection Program,
- to agricultural businesses, under the Agricultural Credit Act and the Feeder Association Loan Guarantee Program, and
- to export businesses, under the Loan Export Program through BC Trade.

Definition of a Guarantee

"A contract of guarantee is one in which there must always be three persons – a principal debtor, whose liability may either be existing or contemplated; a creditor; and a guarantor or surety, who, in consideration of some promise or act of the creditor, promises to discharge the debtor's liability if the debtor should fail to do so."

Source: Anger's *Digest of Canadian Law*, Nineteenth Edition

It also gave a number of ad hoc guarantees, to such businesses as the Pacific National Exhibition and PWA Corporation.

Indemnities

The government may enter into agreements with a variety of people and organizations for many different purposes. Some of these agreements contain an indemnity clause, by which the Province agrees to protect the other party from any loss or harm that may occur to them as a result of the agreement with the Province. For example, if the Province uses someone's land for an access road and a third party is injured on the access road and sues the landowner, the Province, under an indemnity agreement, would compensate the landowner for any loss suffered.

Between April 1, 1991, and March 31, 1994, the government gave out more than 250 indemnities.

The wording of most indemnities is open–ended. For example, "The Province will indemnify and save harmless the contractor, its servants, employees, and agents from and against any and all losses, claims, damages, actions, causes of action, costs and expenses that the contractor may sustain, incur,...." In some cases, the indemnity may be provided only for a limited time or up to a certain amount of money, but more often the potential liability arising from the indemnity is not limited.

This report is written in two sections: one on guarantees and the other on indemnities. The basic requirements for the review, control and approval of guarantees and indemnities are similar. However, the benefits given by the Province are significantly different and our findings regarding each could not easily be combined.

Definition of Indemnity

"to indemnify is to make good a loss which one person has suffered in consequence of the act or default of another; and, the operation of making good the loss is called indemnification."

Source: Dictionary of English Law

Guarantees

Total outstanding government guarantees amounted to approximately $4.2 billion as of March 31, 1994. The majority of this consists of long–term debentures issued by Crown corporations ($2.8 billion) and health and educational institutions ($1 billion). In general, these long–term debentures were issued a number of years ago, when the corporations or institutions were being set up. The amounts outstanding are being drawn down each year, and no new amounts are being issued. Student loan guarantees accounted for $200 million and the British Columbia Home Mortgage Assistance Program accounted for approximately $100 million. These two programs are for personal, rather than commercial, purposes. The remainder included approximately $100 million of commercial loan guarantees, the focus of this audit.

Guarantee Programs

As of March 31, 1994, the outstanding commercial guarantees rested with six major commercial loan guarantee programs — Small Business Assistance Program, Business Expansion Program, Job Protection Program, *Agricultural Credit Act*, Feeder Association Loan Guarantee Program and Loan Export Program — as well as with a number of ad hoc guarantees.

Exhibit 3.1 shows the relative size of each guarantee program as a percentage of the total amounts approved during the life of all programs. It also compares the relative size of each program in dollars to the relative size in number of guarantees given.

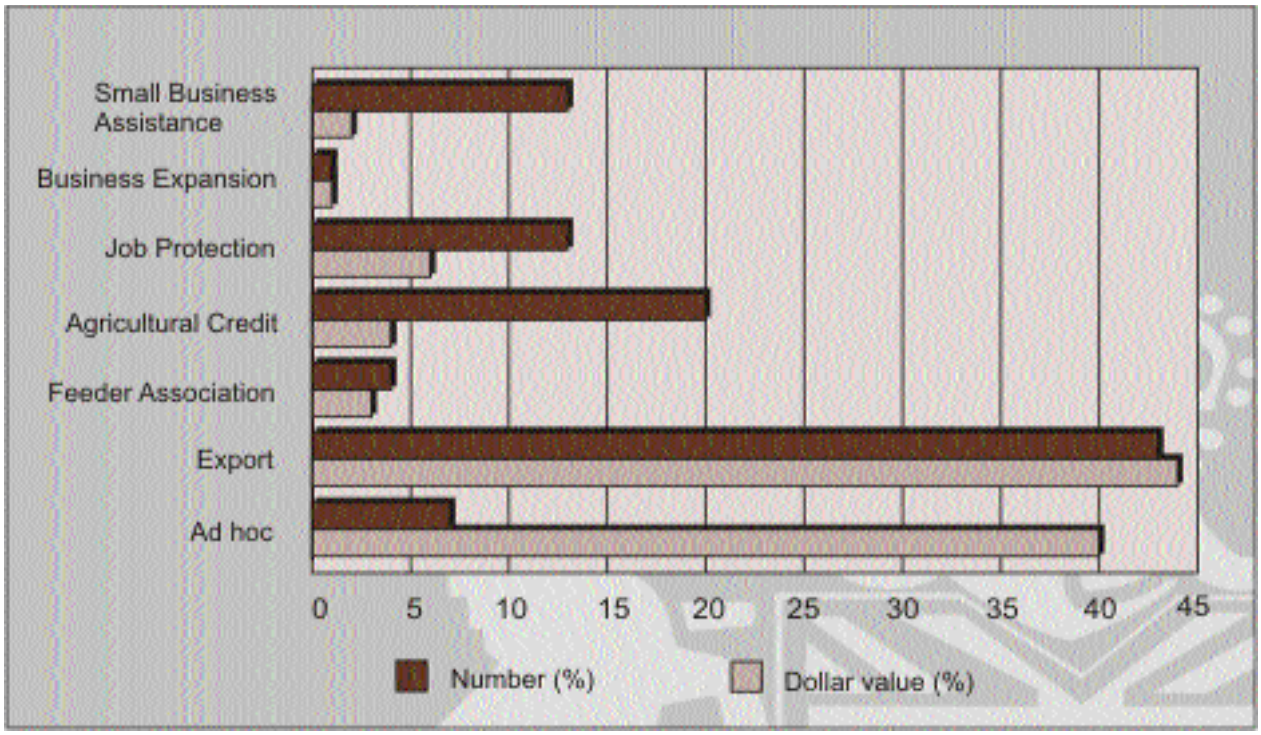
For the guarantee programs we looked at, a total of $120 million in guarantees have been issued over the life of the programs ($86 million in the three–year period covered by our audit). Half of these guarantees are still outstanding and approximately $53 million have expired or relate to loans which have been fully repaid. Claims have been paid for the remaining $8 million, although the amounts have usually only been a portion of what was initially authorized.

Guarantees are usually approved by the ministry responsible for the program unless the dollar amount is such that additional approval is required. Ad hoc loan guarantees may be given by any ministry with appropriate authorization. Once a guarantee has been given, its monitoring and administration becomes the responsibility of the Loans Administration Branch of the Ministry of Finance and Corporate Relations. The exception is the guarantees given by BC Trade; those are administered by that corporation.

The Small Business Assistance Program is currently the responsibility of the Ministry of Small Business, Tourism and Culture. It was initially set up by the Ministry of Economic

Exhibit 3.1

Commercial Loan Guarantees by Program, Given over the Life of the Program



Source: Government of British Columbia

Development, Small Business and Trade, which no longer exists. This program is designed to encourage the establishment, expansion and modernization of small businesses in the Province by providing direct loans for capital expenditures and loan guarantees for working capital loans. During the period covered by our audit, $357,000 in guarantees were given in this program.

The objectives of the program are threefold: to provide businesses with easier access to commercial sources of working capital funding; to promote and support firms that are judged by commercial lenders to be viable but lacking in sufficient collateral security to meet normal lending criteria; and to compensate for regional disparities in the availability of financing throughout the Province.

Guarantees are considered up to a maximum provincial liability of $100,000 each, for a term of up to five years. They are also limited to 75% of the loan amounts for projects located within the Greater Vancouver Regional District (GVRD) and to 85% for projects located outside the GVRD.

The Business Expansion Program is administered by the Ministry of Employment and Investment. This program was also set up by the Ministry of Economic Development, Small Business and

Trade. It is similar to the Small Business Assistance Program, but the assistance is directed towards medium to large–scale projects in the manufacturing, value–added processing and advanced technology sectors in British Columbia. The minimum guarantee that will be considered is $100,000. The term and percentage of the loan guaranteed are the same as for the Small Business Assistance Program. During the period covered by our audit, $1.3 million in guarantees were given in this program.

The Job Protection Program is not specifically for loan guarantees, but guarantees may be provided as part of an economic plan to minimize job loss or to preserve, restore and enhance the competitiveness of business enterprises in British Columbia and the global marketplace. The program, administered by the Ministry of Employment and Investment, includes a subset of loan guarantees known as the Elk Valley Small Business Initiative. Under this initiative, the Province provided assistance to small businesses in the area when Westar Mines declared bankruptcy. Because the *Job Protection Act* does not give specific authority to grant loan guarantees, those given under this program must still be authorized under the *Financial Administration Act*. During the period covered by our audit, $6.7 million in loan guarantees were given.

The *Agricultural Credit Act* is administered by the Ministry of Agriculture, Fisheries and Food. It provides for loan guarantees to be given to farm operators for certain specified purposes, including purchase of livestock, land and buildings or agricultural equipment; development of a water supply; construction or improvement of farm buildings; consolidation or rearrangement of liabilities; or clearing, breaking, irrigating, draining, dyking or fencing of land. The maximum amount of principal for an individual guarantee is $300,000.

The Feeder Association Loan Guarantee Program, also administered by the Ministry of Agriculture, Fisheries and Food, helps British Columbia residents to establish feeder associations. Under this program, a group of livestock farmers can form an association and obtain a line of credit. The Province guarantees 25% of that amount. The association in turn lends amounts of up to $100,000 to individual members to purchase feeder cattle and sheep which are fed on member farms or in feedlots. When the livestock are sold, the money is repaid to the association. This program issued $3.5 million in guarantees during the three years ending March 31, 1994.

The Export Loan Guarantee Program is administered by BC Trade under the *Trade Development Corporation Act* and its related regulation. The objective of this program is to help companies in British Columbia finance their completion of orders prior to shipment out of the Province. The corporation guarantees 85% of a working capital loan up to a maximum of $2.5 million per company. BC Trade issued $39.7 million in loan guarantees

during the period covered by our audit.

Ad hoc guarantees may be given for any purpose and are usually for significant amounts (over $1 million). In the three years ending March 31, 1994, four ad hoc guarantees were issued, having a total value of $34.4 million.

Programs such as these change over time as new needs are identified. As of March 31, 1994, guarantees were no longer being approved under the Small Business Assistance Program, the Business Expansion Program, or the *Agricultural Credit Act*. However, new guarantee programs are being considered.

Audit Scope

We looked at commercial guarantees given by government ministries and government corporations between April 1, 1991, and March 31, 1994. We looked to see whether these guarantees had been approved and controlled in accordance with the requirements of the *Financial Administration Act* and other applicable statutes, the *Guarantees and Indemnities Regulation*, and the related Treasury Board policies. Specifically, we wanted to see whether:

- ministries had established and documented their procedures for the review, control and approval of guarantee requests;
- applications for guarantees contained certain required information;
- risk assessments were completed and contained all the required information;
- guarantees were reviewed by legal counsel before being submitted for approval;
- guarantees were approved by appropriate authorities;
- the Ministry of Finance and Corporate Relations maintained a central record of all guarantees given by ministries and government corporations;
- ministries exercised any rights government has, in consultation with legal counsel, when claims were paid out; and
- the Minister of Finance and Corporate Relations had tabled the required annual report in the Legislature.

We reviewed a random sample of files at the Loans Administration Branch of the Ministry of Finance and Corporate Relations and at the originating ministries. We also had discussions with staff at the branch and the ministries. We wrote to the senior financial officer of each ministry to find out whether they had any policies and procedures in place for guarantees. In addition, we contacted a random sample of financial institutions in the Province to find out whether they had given any loans that were guaranteed by the Province. We also wrote to the chief financial officer of each active government organization included in the Province's summary financial statements to determine whether the organization had given any loan guarantees since April 1, 1991.

We did not look at the non–commercial loan guarantees given under the Student Loan Program or the Home Mortgage Assistance Program. Both of these involve a large number of relatively small loan guarantees and eligibility for the guarantees is automatic when certain criteria are met. They are significantly different in nature from the other loan guarantee programs administered by the Province.

Our audit sample consisted of 26 loan guarantees, accounting for a total value of $44 million, given by the Province between April 1, 1991 and March 31, 1994. We sampled at least one guarantee for each program or Act under which guarantees had been given since April 1, 1991. Although we identified 27 Acts which authorized guarantees, no guarantees had been given under most of them during the period covered by our audit. Consequently, our samples only included guarantees given under the *Financial Administration Act* and the *Agricultural Credit Act*.

In determining whether guarantees given under the Export Loan Program complied with the requirements of the legislation, we did not directly test any guarantees given under the *Trade Development Corporation Act*. Instead, we relied on the work performed recently by the Internal Audit Branch of the Office of the Comptroller General, which covered the period from July 1989 to October 1993.

Overall Observations

Overall, we found that guarantees were being approved by an appropriate authority in compliance with the *Guarantees and Indemnities Regulation*, and were being controlled and reported in compliance with the Treasury Board policies. However, the approval process, as set out in Treasury Board policies, was not being adequately complied with.

Specifically, we found the following:

- Ministries that administered guarantee programs had established and documented procedures for those programs. Only one ministry had documented procedures for the review, control and approval of ad hoc guarantee requests.
- All of the submissions we looked at contained the required information.
- Eighteen of the submissions we looked at contained a risk assessment. However, none of them contained all of the components required by Treasury Board policies.
- Only 16 of the 26 guarantee agreements we looked at had evidence of a legal review prior to approval.
- All of the guarantees we looked at, except for those given under the Feeder Association Loan Guarantee Program, were appropriately approved.
- The Ministry of Finance and Corporate Relations does not maintain a central record of all guarantees given by ministries and government corporations.
- Claims were paid out only after the government had claimed ownership of all security used as collateral.

- An annual report of guarantees issued during each year is tabled as required. However, the report title does not accurately describe its contents.

Audit Findings

Procedures

Treasury Board policy requires that ministries establish and document procedures for the review, control and approval of guarantee requests.

We contacted the senior financial officer of each ministry to find out whether they had such documented procedures.

We found that the three ministries responsible for currently existing guarantee programs do have guidelines in place for those programs. They also have a formal protocol agreement with the Loans Administration Branch of the Ministry of Finance and Corporate Relations which provides for the control of guarantees once they have been issued.

Most ministries responded that they did not normally give guarantees and therefore had not developed any procedures for handling them. Only one ministry had written procedures covering ad hoc guarantees. Another had no detailed written procedures, but included approval of guarantees in its spending authority matrix. Four ministries commented that they were familiar with Treasury Board's requirements for guarantees. One of these told us that any guarantees would be referred to the senior financial officer prior to approval. Six ministries are in the process of developing their own policies and procedures manuals and plan to include a section on the review, control and approval of guarantees.

As any ministry may have occasion to give an ad hoc guarantee, we believe that even ministries which do not normally give guarantees, and are therefore least familiar with the requirements for their review and approval should have written procedures to use for reference.

We recommend that the Ministry of Finance and Corporate Relations reinforce the Treasury Board requirement that ministries giving guarantees have documented procedures for the review, control and approval of ad hoc guarantees. An alternative would be to expand the Treasury Board policies to include detailed guidance as to the review, control and approval of guarantees within ministries.

Content of Submissions

Treasury Board policy requires that submissions for loan guarantees include the name and address of the person guaranteed, the amount of the guarantee, any conditions attached to the guarantee, collateral held or assigned to secure the guarantee, details of the debt or other obligation guaranteed, and a risk analysis.

All of the submissions we looked at contained the required information.

Risk Assessments

A suggested Risk Assessment Checklist is included in the government's Financial

Administration Operating Policy Manual. This list is to be used as a starting point for assessing risk and is not intended to be exhaustive. The manual states that the checklist should be modified where appropriate. All risk analyses should contain, as a minimum, the information included in the checklist.

The checklist contains five sections:

- risk factors, which include corporate factors (such as credit rating, five–year business plan, standard financial ratios, past performance, competition, type of business and associated risks, and assessment of management capability), market factors (such as trends, stability of market, and influence of technological changes) and environmental factors (such as industry outlook, general economic outlook, and likelihood and possible effects of changes in interest rates, exchange rates, tariffs and quotas).
- overall risk assessment – a judgmental rating of low, medium or high;
- most likely case scenario – the most probable size of payout if required;
- worst case scenario – the maximum possible payment that may have to be made; and
- grant option – an assessment of whether a grant should be provided instead of a guarantee and, if so, how large it should be.

Eighteen of the submissions we looked at contained some sort of risk assessment.

One submission, relating to the guarantee to set up the Working Opportunity Fund, did not include a risk assessment. However, because that fund was established before individual investors were known, a separate risk assessment for the associated guarantee was impracticable.

The seven Feeder Association guarantee submissions also did not contain risk assessments. However, the Treasury Board submission for approval of the Feeder Association Loan Guarantee Program stated that none of the feeder programs in other provinces had ever had a defaulted loan. The feeder loans are protected by an insurance fund set up for each association and collateral provided by the feeder herd itself. This implies that the risk of default under this program is very small.

In general, the risk assessments for the ad hoc guarantees were less detailed than those in specific programs for which application forms were required. In addition to risk assessments, submissions for ad hoc guarantees also included information on such things as the number of jobs that would be protected and the amount of tax revenue that would be protected. For example, the $5 million loan guarantee to Cassiar Mining Corporation was expected to protect approximately 400 jobs and $5.7 million in provincial tax revenues annually. For many ad hoc guarantees, the risk of the loan

defaulting is not the primary criterion for approval.

Except as noted above, all of the submissions we looked at contained an assessment of the corporate and market factors. Any assessment of the environmental factors, however, focused on the "green" environment rather than the business environment as required by Treasury Board policy.

Only seven of the submissions we looked at included an overall risk assessment. All five of the submissions for guarantees given under the *Agricultural Credit Act* contained an overall risk assessment in the final submission from the Deputy Minister to the Minister, who approves the guarantees. However, in one case, we found that the submission to the minister stated that the risk was moderate, even though the background information prepared by the credit manager and the credit analyst at the ministry stated that there was a higher than average level of risk associated with this loan. No explanation for the change in risk assessment was documented. Of the other two submissions that contained an overall risk assessment, one was given under the Job Protection Program and one under the Business Expansion Program.

Only one of the submissions we looked at (for a guarantee under the *Agricultural Credit Act*) included a most likely case scenario. One ministry commented that, in some programs, guarantees were only given to viable businesses that were expected to be able to repay the loan, so the most likely case scenario was always repayment in full. However, we could find no evidence that this fact had been documented or otherwise communicated to the person in each ministry approving the guarantees.

A worst case scenario was assessed for only two of the submissions in our sample. Both of these submissions were for *Agricultural Credit Act* guarantees that included an analysis of the effects of changes in crop prices on the borrower's ability to pay back the loan. Again, the same ministry commented that the worst case scenario was always the full amount of the guarantee plus interest. In fact, however, the full amount of the guarantee is rarely paid out, as the business is likely to have paid back at least a portion of the loan before defaulting. Furthermore, in most cases, the Province does not give guarantees unless the borrower has provided some sort of collateral that must be realized before any claim can be made on the guarantee.

None of the submissions addressed the issue of whether a grant would have been more appropriate.

Ministry staff informed us that, in general, the grant option is not considered because the application is submitted under a loan guarantee program and it is assumed that this form of assistance is what the applicant requires. Since any given program can only provide certain kinds of assistance, a person making a request for a loan guarantee would either get the guarantee or be turned down under that program. It would then be up to the

applicant to find another program under which they might be eligible. Consideration of the grant option is therefore only really relevant for ad hoc guarantees.

In summary, all guarantee submissions we examined contained the basic elements of the required information. None of them, however, included a risk analysis that met all the content requirements in the Treasury Board policy. The sections of the risk assessment checklist most commonly omitted were the summary sections: overall risk assessment, most likely case scenario, and worst case scenario. As these sections provide the "bottom line" to the person ultimately approving the guarantee and yet take very little time to complete once the detailed risk factors have been documented, we believe they should always be included in the submission.

We recommend that the Ministry of Finance and Corporate Relations reinforce the requirements of Treasury Board policies regarding the content of loan guarantee submissions. Ministries that have guarantee programs should ensure that their approval checklist includes all the components required by Treasury Board policy. When the risk assessments for all individual guarantees approved under a program are the same and the ministry wishes to avoid repeating the same risk assessment in each individual submission, the ministry should get Treasury Board approval for the general assessment and the right not to provide risk assessments in each individual submission.

Legal Review

Treasury Board policy requires that all guarantees be reviewed by the ministry's legal counsel before being submitted for approval.

For 16 guarantees in our audit, we found evidence that the agreement had been reviewed by legal counsel before being approved. These included all submissions for ad hoc, Feeder Association and Business Expansion Program loan guarantees, and one submission under the Job Protection Program.

For the remaining 10 guarantees, with a total value of $810,475, we could find no evidence of legal review prior to approval. Five of these guarantees, all given under the *Agricultural Credit Act* used a standard agreement, but neither ministry staff nor the ministry's solicitor could confirm that it had been reviewed or drafted by legal counsel. For one of the submissions under the Job Protection Program and all of the Small Business Assistance Program guarantees, the ministry responsible at the time (Economic Development, Small Business and Trade, which no longer exists) used what it considered to be its standard agreement for all small business guarantees under $100,000. This agreement had been developed by the Ministry of Attorney General for a previous loan guarantee program. However, legal counsel was not informed that the agreement was being used for other programs, so could not comment on whether it was appropriate for the new circumstances.

We recommend that ministries document the source of standard agreements used in guarantee programs, and consult with legal counsel when they intend to expand the use of standard agreements developed for earlier programs.

Approval

The *Guarantees and Indemnities Regulation* states that Minister approval is required for individual guarantees up to $100,000; Treasury Board approval is required for guarantees between $100,000 and $1 million; and Lieutenant Governor in Council approval is required for all guarantees over $1 million. The Minister of Finance can approve guarantees of any size.

Nineteen of our sample guarantees were appropriately approved. Five of these were approved in compliance with the *Agricultural Credit Act*, and the remaining 14 were approved in compliance with the *Financial Administration Act*.

Seven Feeder Association loan guarantees with a total value of $2.75 million, given under the *Financial Administration Act*, were not appropriately authorized. They were approved by the Minister of Agriculture, Fisheries and Food rather than by Treasury Board or the Minister of Finance and Corporate Relations.

In September 1990, Treasury Board approved a submission to establish the Feeder Association Loan Guarantee Program to provide guarantees to different feeder associations up to a total of $2.5 million. (The limit has since been raised to its current ceiling of $4.25 million.) However, this is not the same as approving the individual loan guarantees. The ministry understood that this meant its minister had the authority to approve individual loan guarantees as long as the total authorized did not exceed the $2.5 million ceiling established by Treasury Board for the program. In fact, this was not the case.

We recommend that the Ministry of Agriculture, Fisheries and Food obtain appropriate approval for all of its guarantees under the Feeder Association Loan Guarantee Program.

Claims Paid Out

Treasury Board policy requires that when the government makes a payment in respect of a guarantee, ministries must exercise any rights the government may have, in consultation with Crown Counsel. One of the objectives of the policy is to establish standard procedures to be taken when payment of a guarantee becomes necessary.

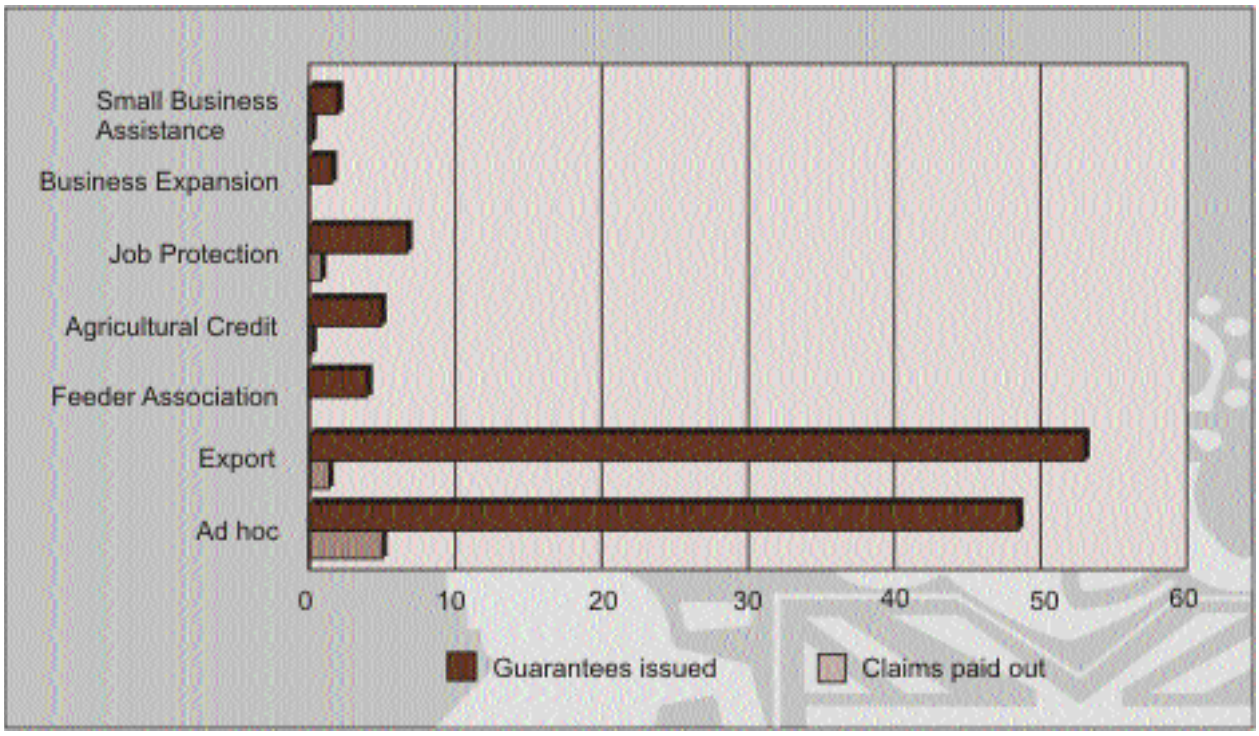
Exhibit 3.2 shows the guarantees given during the life of each program we looked at and compares that amount to the claims paid out in the five years since April 1, 1989.

In practice, it is the Loans Administration Branch, rather than individual ministries, that is responsible for making all payments for defaulted guaranteed loans and collecting on any security. The Loans Administration Manual includes a list of requirements to be met before a payout is made, as well as a disbursement checklist that may be used to deal with claims.

Exhibit 3.2

Comparison of Guarantees Issued to Claims Paid Out

1990 – 1994 ($ Millions)



Source: Government of British Columbia

We looked at all nine loan guarantees paid out in the programs included in our audit sample to determine whether this checklist had been followed. We found that all files contained evidence that a sufficient investigation had been done prior to payout, such as correspondence with the lending institution and the borrowers and notes of telephone conversations. Although Crown Counsel did not appear to have been consulted in every case, we did find that they were contacted without hesitation when difficulties over payment were encountered.

One concern we had, however, was that the documentation included in the file varied from one loans officer to another. Some staff documented the results of their investigation in a memo to file listing the information specified in the manual and the evidence obtained. Others included the sample checklist, checking off the steps as they had been completed. Others did not summarize the results of their investigation at all, explaining to us that this is not a requirement.

We recommend that the Loans Administration Branch establish consistent procedures for summarizing the results of its investigations prior to paying out any guarantee claims.

Central Records

Treasury Board policy requires the Ministry of Finance and Corporate Relations to maintain a central record of all guarantees given by ministries and government corporations. The Loans Administration Branch maintains records of all the loans it administers, but it does not administer all the loan programs in government. As at March 31, 1994, the loans not included on the Loans Administration list were as follows:

- the Ministry of Small Business, Tourism and Culture has a list of the outstanding guarantees given under the Business Start–Up Program ($3.9 million),
- the British Columbia Trade Development Corporation has a list of the outstanding guarantees given under the Export Loan Program ($19.5 million), and
- the Okanagan Valley Tree Fruit Authority maintains a list of the outstanding guarantees given by them under their enabling legislation ($400,000).

Although the Ministry of Finance and Corporate Relations does not maintain the required list of all guarantees given by ministries and government corporations, it is aware that BC Trade and the Ministry of Small Business, Tourism and Culture have loan guarantee programs. It obtains a list of guarantees from these entities at each year–end for inclusion in the government's financial statements.

To determine whether all guarantees given by the Province were recorded by the Ministry of Finance and Corporate Relations, we contacted 27 government corporations included in the government's summary financial statements and asked for a list of any guarantees given by them since April 1, 1991. As well, we sent letters to a random sample of 252 financial institutions in the Province, asking whether they held any loans guaranteed by the Province.

We compared the responses of these institutions to Office of the Comptroller General's detailed list supporting the Statement of Guaranteed Debt in the government's Consolidated Revenue Fund financial statements. We found three main differences:

- The Okanagan Valley Tree Fruit Authority is the only entity that maintains a record of the guarantees it issues.
- One bank reported a loan of which $127,500 was guaranteed by BC Trade. According to BC Trade, the guarantee had expired (although there is no expiry date in the guarantee agreement) and therefore the corporation does not include it in its list to the Province of outstanding guarantees at year–end. Both parties are aware of this discrepancy.
- One credit union listed a $50,000 loan to an improvement district as being guaranteed by the Province. Although this is not, in fact, a guarantee, financial institutions consider such loans to improvement districts to be guaranteed, as they will be repaid when the

district receives funding from the Province. The ministry wrote to the credit union to re–emphasize that these loans are not guaranteed by the Province.

We recommend that the Ministry of Finance and Corporate Relations maintain the required list of all outstanding guarantees given by ministries and government corporations.

Report Tabled by the Ministry of Finance and Corporate Relations

The *Financial Administration Act* requires the Ministry of Finance and Corporate Relations to table an annual report of all guarantees and indemnities issued during the year with either Treasury Board or Lieutenant Governor in Council approval. No guarantees were approved by either body during the three years covered by our audit.

Nevertheless, the ministry tables a report each year entitled "Guarantees and Indemnities Issued and Authorized by Treasury Board or the Lieutenant Governor in Council for the Fiscal Year Ended March 31, 19xx." It lists most loan guarantees issued during the fiscal year, whether or not they required approval by Treasury Board or the Lieutenant Governor in Council. For example, the 1994 report lists all loan guarantees given by the Ministry of Employment and Investment, none of which was larger than $50,000. In each year, the report also includes an amount for guarantees given for student loans and those under the First Citizens' Fund. Although including these amounts provides additional information to the public, none of these loan guarantees require Treasury Board or Lieutenant Governor in Council approval, so the report content does not match its title.

The requirement that the report contain guarantees and indemnities approved by Treasury Board or the Lieutenant Governor in Council is presumably so that high dollar value items are reported publicly. However, the Minister of Finance and Corporate Relations can approve guarantees and indemnities of any amount. Thus, for example, the largest loan guarantee given by the Province in the last three fiscal years – a $20 million loan guarantee given to PWA Corporation in December of 1992 — did not need to be included in the tabled report because it was approved directly by the Minister of Finance, and not by Treasury Board or the Lieutenant Governor in Council. Ministry staff informed us that they would normally have included this guarantee in the report, but it was omitted in error.

We reviewed these reports for the fiscal years ending in 1992, 1993, and 1994. For the first two years, the loan guarantees given under the Feeder Association loan program were recorded at the full amount of the loans themselves, rather than the amount of the guarantee, which is 25% of the total loan. This error was corrected in the 1994 report.

We recommend that consideration be given to amending the Financial Administration Act *to require that all guarantees given by the Province be included in the annual report.*

Other Observations

Conditions in Approved Submission Are Contained in Agreement

In most cases, submissions for loan guarantees contain conditions which must be included in the guarantee agreement. The most common condition is the security that must be obtained by the bank. Some submissions contain conditions which must be met before the guarantee is approved. For example, the guarantee for the Pacific National Exhibition could not be approved until the Province had received assurance from the City of Vancouver that Playland would remain in operation for a period long enough to pay off the loan.

For all of our audit samples, we reviewed the submissions, whether they were detailed submissions under the specific programs we looked at, or Cabinet and Treasury Board submissions for ad hoc guarantees. The Office of the Comptroller General, in its audit of BC Trade's Export Loan Guarantee Program, noted that the signed agreement for one guarantee omitted a condition that had been in the approved submission. However, in all other cases, any conditions in the submission were either met before the guarantee was signed or, in the case of security for the loan, included in the guarantee agreement.

Public Reporting

A recent Public Sector Accounting Pronouncement issued by the Canadian Institute of Chartered Accountants, *Accounting for Government Loan Guarantees,* states that government financial statements should disclose in notes or schedules the nature and terms of significant classes of loan guarantees. Information that should be disclosed includes: the authorized limit, the principal amount outstanding, the amount of provision for losses, and general terms and conditions. Currently the government only discloses the net outstanding guaranteed debt. This is defined as the gross principal debt less sinking fund balances, and represents the total amount of contingent liability of the government arising from relevant guarantees.

We recommend that the government consider including the additional information recommended by professional pronouncements in its Statement of Guaranteed Debt contained in the Consolidated Revenue Fund financial statements.

Guarantees Dependent on Future Government Assistance for Repayment

For all 26 sample guarantees, we ran a computer program to determine whether any payments had been made by the Province to the guarantee recipients.

We found payments made to two of the parties in our samples. There was no indication that any of these payments were related to the government guarantees, and none

of the payments were significant compared to the amount of the loan guarantee.

We concluded that the government has not given out loan guarantees to entities which were dependent on future government assistance for repayment.

Municipalities, Universities, School Districts and Hospitals

We reviewed the Statements of Financial Information required by the *Financial Information Act* for municipalities, universities, colleges, school districts and hospitals to determine whether they had issued any guarantees.

Based on the information we reviewed we found that municipalities, universities, school districts and hospitals do not issue guarantees in the normal course of doing business.

Other Legislation

Twenty–seven statutes, in addition to the *Financial Administration Act*, allow various organizations to provide guarantees. We compared the requirements of the various pieces of legislation to see if they were consistent (Exhibit 3.3). Most statutes that permit guarantees make provision for the government to guarantee debt entered into by government corporations. In these cases, the Lieutenant Governor in Council's approval is required. However, some permit the organization to guarantee a third party's debt and allow the responsible Minister or the organization to approve the guarantees. We found that the legislative requirements for approving guarantees were consistent for similar circumstances.

Exhibit 3.3

Legislative Requirements for Approving Guarantees

Guarantees Given to Government Corporations	Guarantees Given to Individuals and Independent Organizations
Guaranteed by the Crown, on terms approved by the Lieutenant Governor in Council *British Columbia Buildings Corporation Act* *British Columbia Railway Finance Act* *British Columbia Transit Act* *Dyking Authority Act* *Educational Institution Capital Finance Act* *Ferry Corporation Act* *Hospital District Act* *Hospital District Finance Act* *Hydro and Power Authority Act* *Insurance Corporation Act* *Ministry of Transportation and Highways Act* *Municipal Act* *Pacific North Coast Native Cooperative Act* *Petroleum Corporation Act* *School Act* *School District Capital Finance Act* *System Act*	Authorized by the Minister, with the approval of the Lieutenant Governor in Council *Ministry of Energy, Mines and Petroleum Resources Act* Guarantee issued and approved by the Corporation *Trade Development Corporation Act* *Okanagan Valley Tree Fruit Authority Act* Approved by the Lieutenant Governor in Council and a two–thirds majority of shareholders *British Columbia Railway Act* Guarantee given by the Minister responsible for the statute *Special Accounts Appropriation and Control Act* (First Citizens' Fund) *Agricultural Credit Act* *Farm Product Industry Act* Authorized by the Lieutenant Governor in Council *Farm Income Insurance Act* *Farm Distress Assistance Act* Criteria for approval set by regulation *Home Mortgage Assistance Program Act*

Indemnities

An indemnity is a promise to make good a loss that one person may suffer as a result of the act or omission of another. It transfers financial risk from the person being indemnified to the person given the indemnity.

Some examples of indemnities given by the Province over the last few years include:

- to a ranch company for the release of a land claim,
- to a hospital for a Ministry of Health employee to get some practical experience,
- to British Columbia Hydro and Power Authority to use a BC Hydro right–of–way for a road in the Peace River District, and
- to Esquimalt and Nanaimo Railway Company and Fording Coal Limited for reclamation work at Mount Washington Copper Mine.

Indemnities can expose the government to significant risk. They are often open–ended, with no specified limit to the amount of financial exposure or length of time they are in effect. In addition, the party giving the indemnity – in this case the government – may be asked to accept a risk over which it has no control.

When a contract is drawn up, an indemnity clause is often included as a means of transferring risk. Many of the standard contracts drawn up by the government include a standard clause in which the contractor is required to indemnify the government for any losses the contractor may incur as a result of their activities in carrying out the agreement. Likewise, a contract drawn up by a contractor often includes a clause requiring the government to indemnify the contractor. For this reason, ministries encourage the use of their own standard contracts, rather than the contractors' agreements, whenever possible.

Audit Scope

We looked at indemnities given by ministries and government corporations between April 1, 1991 and March 31, 1994. Our purpose was to assess whether these indemnities had been reviewed, controlled and approved in compliance with the *Financial Administration Act*, the *Guarantees and Indemnities Regulation*, and the related Treasury Board policies. Specifically, we wanted to see whether:

- ministries and government corporations had established and documented procedures for the review, control and approval of indemnities;
- indemnities were approved by appropriate authorities;
- indemnities, where possible, contained dollar limits and an expiry date; and
- the Risk Management Branch maintained a central record of all indemnities that have

received Treasury Board approval.

We did not look at indemnity programs managed by the government, such as the Hospital Protection Program which indemnifies health care facilities in the Province, or at the indemnification of government–appointed members of agencies, boards and commissions.

Without a detailed knowledge of the negotiations leading to each indemnity being granted, we found it impossible to determine whether a dollar limit or expiry date could have been included. Therefore the section of our report on this requirement only includes information about the extent to which we found these restrictions included in indemnity clauses.

Overall Observations

We were unable to determine whether all indemnities had been appropriately approved. We found a lack of clear understanding in government organizations about the nature of indemnities. This situation suggests to us they may be unable to identify an indemnity, and consequently not obtain the necessary approval even when they are aware of the requirements.

Most ministries and government corporations did not have any policies and procedures to ensure that indemnities were always reviewed, controlled and approved.

Approximately half of the indemnities we looked at contained an expiry date, but very few of them limited the dollar value of the liability. We found that, in most cases, the nature of an indemnity is such that it would be impossible to limit the liability to a certain amount. It would also be extremely difficult, if not impossible, to estimate the potential liability.

Audit Findings

Procedures

Treasury Board policy requires all ministries and government corporations to establish and document procedures for the review, control and approval of indemnities.

General guidance for the approval and reporting of indemnities is contained in the *Guarantees and Indemnities Regulation* and expanded on in Treasury Board policies which are included in the government's Financial Administration Operating Policy Manual. We believe, however, that ministry–specific procedures are still necessary. Although many ministries have contract management staff who are familiar with these central agency requirements, agreements or types of contracts are processed through other parts of the ministry by staff who are not as knowledgeable. In addition, the central requirements do not include procedures for the review and control of indemnities within ministries, or state who in the ministry should approve such clauses.

To determine whether procedures existed, we contacted the senior financial officer of each ministry and wrote to the chief financial officers of 27 government corporations included in the government's summary financial

statements. We did not contact inactive or defunct organizations or those whose only function is to provide financing, such as the Capital Financing Authorities.

We found that most ministries and government corporations did not have any procedures for the review, control and approval of indemnities. Specifically, our findings were as follows:

- Six ministries had documented procedures for the approval of indemnities, although only two ministries (Health and Energy, Mines and Petroleum Resources) had policies that addressed the control of indemnities after they had been approved, requiring a copy of the approved contract to go to the senior financial officer.
- Twelve ministries said that they had no such procedures documented, although eight of them plan to document them within the next year. Three of these stated that they followed Treasury Board's policies, or that they relied on some central agency such as the Office of the Comptroller General or legal counsel when dealing with indemnities.
- Five of the ministries without documented procedures stated that they had, nevertheless, established procedures. Two ministries make a practice of using only standard contracts, which do not give indemnities. One of these, and four others, stated that all contracts are reviewed by their senior financial officer or a specific branch in the ministry.
- Five government corporations (British Columbia Hydro and Power Authority, the Insurance Corporation of British Columbia, British Columbia Buildings Corporation, British Columbia Housing Management Commission and British Columbia Transit) have the authority to approve their own indemnities as they are related to the usual business operations of the government corporation, and so have had their policies and procedures for doing so approved by the Minister of Finance and Corporate Relations.
- Four additional corporations (British Columbia Pavilion Corporation, British Columbia Assessment Authority, British Columbia Railway Company and British Columbia Ferry Corporation) had policies governing indemnities, but only British Columbia Pavilion Corporation stated in its policies that Risk Management Branch approval was required. British Columbia Railway Company, British Columbia Assessment Authority and British Columbia Ferry Corporation included an internal approval process in their policies, but did not specifically mention the requirement for Risk Management Branch approval. None of these corporations, however, has been given the authority to approve their own indemnities.
- Eighteen government corporations stated that they had no documented policies or

procedures for the review, control or approval of indemnities.

We recommend that the Ministry of Finance and Corporate Relations issue new guidance to all ministries and government corporations explaining the nature of indemnities and reinforcing the Treasury Board requirement for establishing and documenting procedures for the review, control and approval of indemnities.

Limit of Liability

Treasury Board policy requires that, where possible, indemnities have an expiry date and a dollar limit. We found that in most cases the liability under the indemnity is not quantifiable because of its nature. Therefore, without detailed knowledge of the negotiations that led to each indemnity being provided, it was impossible for us to determine whether a dollar limit or a time limit would have been feasible to set.

Exhibit 3.4 shows the number of indemnities approved by the Risk Management Branch in each of the last three fiscal years. As the exhibit makes clear, approximately half of the indemnities issued each year have an expiry date, but very few have a dollar limit.

Approval of Indemnities

The *Guarantees and Indemnities Regulation* requires that all indemnities be approved either by the Minister of Finance and Corporate Relations or the Director of the Risk Management Branch. Alternatively, government corporations may approve their own indemnities if they have procedures for doing so and those procedures have been approved by the Minister of Finance and Corporate Relations.

We were unable to determine whether all indemnities were appropriately approved. We attempted to identify a population of contracts or agreements that we could test to see if they included indemnities and if so, whether the indemnities were appropriately approved. However, because no central listing of contracts or agreements exists in most ministries, we were unable to do this.

Exhibit 3.4

Summary of Indemnities Given, 1991/92 – 1993/94

Indemnities with expiry dates and dollar limits

	Year of Issuance		
	1991/92	1992/93	1993/94
Total indemnities	72	86	92
Indemnities with expiry date	41	50	45
Indemnities with dollar limit	2	2	3

Source: Risk Management Branch

We also tried to identify contracts containing indemnity clauses by selecting a sample of high dollar value payments. We reviewed a sample of contracts that authorized these payments, but found most of them did not include indemnity clauses.

We then went to several ministries – Health; Attorney General; Transportation and Highways; Energy, Mines and Petroleum Resources; and Employment and Investment. We felt that these ministries were the most likely to have contracts with indemnity clauses. We took a random sample of over 50 contracts from the files at these ministries, and also talked to the contract management staff to determine their procedures for approving contracts. Staff at all of these ministries informed us that they discourage the use of non–standard contracts and do not enter into contracts that include a clause in which the government provides an indemnity. In general, we found that ministries had developed several standard contracts for different situations, and that the majority of contracts we reviewed were standard.

We found only one contract with an indemnity clause that had not been appropriately approved. The Ministry of Attorney General, instead of using its standard contract, had signed a supplier's standard contract, which contained a clause indemnifying the supplier. A further review of indemnities listed by the Risk Management Branch indicated that most are given in agreements that do not involve the government making payment for services.

Some ministries rely on legal counsel at the Ministry of Attorney General to ensure that indemnities are sent to the Risk Management Branch or Treasury Board for the appropriate approval. We had discussions with the supervising solicitors in the Ministry of Attorney General to determine what their procedure was when they received a contract with an indemnity clause in it. Usually, we were told, they either send the contract directly to the Risk Management Branch for approval or return it to the originating ministry with instructions to send it to the Risk Management Branch. They do not produce an executable contract until they have approval either from Risk Management Branch or Treasury Board.

From the 27 government corporations we contacted, we requested a list of the indemnities given since April 1, 1991. We compared these lists to the Risk Management Branch list of indemnities approved during the last three fiscal years. For the 22 government corporations that cannot approve their own indemnities, we identified 59 indemnities given since April 1, 1991. Fourteen of these were not appropriately approved. They were issued by corporations unauthorized to approve their own indemnities, and without approval the Risk Management Branch or the Minister of Finance and Corporate Relations.

We did not perform similar procedures for indemnities given by ministries, since for indemnities

issued during the year, they are only required to report those indemnities approved by the Minister of Finance and Corporate Relations or Treasury Board. Most indemnities provided by ministries are approved by the Risk Management Branch and are therefore reported only on its list.

Our detailed findings for government corporations are as follows:

- Fifteen of the government corporations we contacted had not given any indemnities since April 1, 1991.
- Five government corporations have been given the authority to approve their own indemnities, which therefore do not appear on the list provided by the Risk Management Branch.
- Four government corporations – the British Columbia Health Care Risk Management Society, British Columbia Pavilion Corporation, BC Trade and the Pacific National Exhibition – reported a total of 13 indemnities to us which had not been appropriately approved.
- The remaining three corporations did not report any indemnities to us that had not been appropriately approved, although we found one indemnity, given by the Science Council of British Columbia, that was neither reported to us nor appropriately approved.

Before responding to our requests for information, staff at several corporations contacted us for an explanation of the term "indemnity." This suggests to us that indemnities are being given without proper approval because staff cannot identify indemnities.

We recommend that government corporations be reminded of the requirement that they must obtain the approval of the Minister of Finance and Corporate Relations to have the authority to approve their own indemnities.

Indemnities Given by Government Corporations

To determine whether government corporations adequately controlled the indemnities they issued, we compared the list of indemnities approved by the Risk Management Branch to the lists of current indemnities we requested from the government corporations. Some government corporations could not provide us with a complete list of the indemnities they had issued over the last three years.

- Fifteen corporations had not given any indemnities and so provided us with a nil report.
- Three corporations listed the same indemnities recorded by the Risk Management Branch.
- Four other corporations have the authority to approve their own indemnities, and thus indemnities given by them do not appear on the Risk Management Branch list. We therefore could not verify the completeness of their lists. British Columbia Transit and British Columbia Hydro and Power Authority, both of which have the authority to approve

their own indemnities, could not give us a complete list of the indemnities issued, even though their own policies require them to maintain such a list. However, BC Hydro could provide us with a list of the indemnities given by their properties division, which accounts for the majority of their indemnities.

- Five corporations provided us with an incomplete list of indemnities they had issued in the past three years.

Although there is no specific Treasury Board policy that government corporations maintain a list of indemnities issued, they are required to have procedures for the control of indemnity clauses in contracts.

We recommend that government corporations be required to maintain a list of all indemnities issued, which could be reconciled to the Risk Management Branch list.

Consistency of Legislation

Treasury Board policy requires the Risk Management Branch to maintain a central record of all indemnities that have received Treasury Board approval. However, the *Guarantees and Indemnities Regulation* does not allow Treasury Board to approve indemnities. Approval is restricted to either the Minister of Finance and Corporate Relations or the Director of the Risk Management Branch. The only requirement for Treasury Board to approve indemnities appears in Treasury Board policies. Since Treasury Board policy is subordinate to regulations, clearly it cannot override them.

We recommend that the Guarantees and Indemnities Regulation *and the Treasury Board policies be reviewed and amended as necessary so that they are consistent with each other.*

Year–end Reporting by Ministries

At year–end, ministries are required to report to the Office of the Comptroller General all indemnities approved by Treasury Board or the Lieutenant Governor in Council and issued during the fiscal year. However, as discussed above, the *Guarantees and Indemnities Regulation* does not allow Treasury Board or the Lieutenant Governor in Council to approve indemnities.

Ministries are required to report, on a separate form, all indemnities in place at each year–end. These forms provide the detailed information used as a basis for the contingent liability note in the government's financial statements.

In total, we identified 135 indemnities given by ministries in the past three years, 108 of which were still in effect at March 31, 1994. Only 26 of these latter, however, were reported to the Office of the Comptroller General by the ministries on their year–end reports. Twenty–nine of the unreported indemnities were given by the Ministry of Transportation and Highways, which has not been listing individual indemnities on its year–end report. Its report states only that there are various indemnities in place relating to construction work performed.

Several ministries understood that they did not have to report any indemnities that had been approved by the Risk Management Branch. While this is the case for indemnities approved during the year, it is not the case for indemnities in place at year–end. The Office of the Comptroller General obtains, directly from the Risk Management Branch, a list of all indemnities approved during each year. However, this list does not indicate which indemnities are outstanding at each year–end because only the ministries have information about the expiry of the agreements that contain the indemnities. This information can therefore only be obtained directly from the ministries.

We recommend that ministries keep track of the indemnities they have issued, and their expiry dates, so that they can provide an accurate list of indemnities in place.

Report Tabled by the Ministry of Finance and Corporate Relations

The *Financial Administration Act* requires the Ministry of Finance and Corporate Relations to table an annual report listing all guarantees and indemnities issued during the year with approval of Treasury Board or the Lieutenant Governor in Council. As the *Guarantees and Indemnities Regulation* does not allow either Treasury Board or the Lieutenant Governor in Council to approve indemnities, this reporting requirement is not consistent with the approval requirement.

We found that the list of indemnities in each year's report closely parallels the list of indemnities approved in each year by the Risk Management Branch. However, in the reports we examined, the indemnities listed were those approved by the Risk Management Branch, not by Treasury Board or the Lieutenant Governor in Council.

We also found that the tabled reports contain some indemnities not on the Risk Management Branch list and vice versa.

For each of the three years covered by our audit, the report includes most of the indemnities approved by the Risk Management Branch. The 1992 report also includes one indemnity that the branch informed us was approved by Treasury Board, although there is no indication in the report that it had been approved any differently from the other indemnities on the list. In addition, the Risk Management Branch's records indicate that this indemnity was not actually approved until the next fiscal year, which means it should not have been included in the 1992 report. The 1993 report included three items not listed by the Risk Management Branch. Two of them are not considered to be indemnities by the branch (one is a guarantee, which should therefore have been listed in the report as such) and the other was not approved until November 1993. We found one indemnity that was approved by the Minister of Finance and Corporate Relations in October 1993. It was not listed in the 1994 report.

While we endorse the disclosure of all indemnities in a public report, the current

requirement is for the disclosure of all indemnities requiring approval by Treasury Board.

We recommend that the Financial Administration Act *and regulation be reviewed and amended as necessary, to ensure that the reporting requirements for indemnities are consistent with the approval requirements.*

We recommend that consideration be given to amending the Financial Administration Act *to require that all indemnities approved and issued by the Province be included in the annual report.*

Other Observations

Municipalities, Universities, School Districts and Hospitals

We reviewed the Statements of Financial Information for municipalities, universities, colleges, school districts and hospitals to determine whether they had issued any indemnities. Only one organization disclosed an indemnity in its financial statements. The City of Trail issued a $15 million indemnity to West Kootenay Power, doing so under section 288 of the *Municipal Act*, which requires a ministerial order as approval.

Based on the information we reviewed, we concluded that municipalities, universities, school districts and hospitals do not issue stand–alone indemnities in the normal course of doing business. However, it is possible that they do provide indemnities as an incidental part of a larger contract.

Disclosure of Indemnities

The only disclosure of indemnities we found in the Public Accounts is the following sentence in the Contingencies note: "The government also has contingent liabilities in the form of indemnities, indirect guarantees and outstanding claims. Where indemnities are for explicit quantifiable loans, the amounts are included in the statement of guaranteed debt."

We believe that this sentence does not adequately portray the range and potential liability of the indemnities. Without more description of the types of indemnities, the possible magnitude of these contingent liabilities cannot be understood. For example, the Ministry of Transportation and Highways issues numerous indemnities as part of its business of constructing and maintaining roads throughout the Province and the Ministry of Forests issues numerous indemnities related to tree farm licences. If these major categories of indemnities were described in the Public Accounts, we believe they would be more informative.

While we recognize that it is impossible to put a dollar value on indemnities for disclosure in the government's financial statements, we recommend that a description of some of the major categories of indemnities be included in the note to the financial statements that discloses indemnities.

Summary of Recommendations

Guarantees

The Office of the Auditor General recommends, that:

- *The Ministry of Finance and Corporate Relations reinforce the Treasury Board requirement that ministries giving guarantees have documented procedures for the review, control and approval of ad hoc guarantees. An alternative would be to expand the Treasury Board policies to include detailed guidance as to the review, control and approval of guarantees within ministries.*
- *The Ministry of Finance and Corporate Relations reinforce the requirements of Treasury Board policies regarding the content of loan guarantee submissions. Ministries that have guarantee programs should ensure that their approval checklist includes all the components required by Treasury Board policy. When the risk assessments for all individual guarantees approved under a program are the same and the ministry wishes to avoid repeating the same risk assessment in each individual submission, the ministry should get Treasury Board approval for the general assessment and the right not to provide risk assessments in each individual submission.*
- *Ministries document the source of standard agreements used in guarantee programs, and consult with legal counsel when they intend to expand the use of standard agreements developed for earlier programs.*
- *The Ministry of Agriculture, Fisheries and Food obtain appropriate approval for all of its guarantees under the Feeder Association Loan Guarantee Program.*
- *The Loans Administration Branch establish consistent procedures for summarizing the results of its investigations prior to paying out any guarantee claims.*
- *The Ministry of Finance and Corporate Relations maintain the required list of all outstanding guarantees given by ministries and government corporations.*
- *Consideration be given to amending the* Financial Administration Act *to require that all guarantees given by the Province be included in the annual report.*
- *The government consider including the additional information recommended by professional pronouncements in its Statement of Guaranteed Debt, contained in the Consolidated Revenue Fund financial statements.*

Indemnities

The Office of the Auditor General recommends, that:

- *The Ministry of Finance and Corporate Relations issue new guidance to all ministries and government corporations explaining the nature of indemnities and reinforcing the Treasury Board requirement for establishing and documenting procedures for the review, control and approval of indemnities.*
- *Government corporations be reminded of the requirement that they must obtain the approval of the Minister of Finance and Corporate Relations to have the authority to approve their own indemnities.*
- *Government corporations be required to maintain a list of all indemnities issued, which could be reconciled to the Risk Management Branch list.*
- *The* Guarantees and Indemnities Regulation *and the Treasury Board policies be reviewed and amended as necessary so that they are consistent with each other.*
- *Ministries keep track of the indemnities they have issued, and their expiry dates, so that they can provide an accurate list of indemnities in place.*
- *The* Financial Administration Act *and regulation be reviewed and amended as necessary, to ensure that the reporting requirements for indemnities are consistent with the approval requirements.*
- *Consideration be given to amending the* Financial Administration Act *to require that all indemnities approved and issued by the Province be included in the annual report.*
- *While we recognize that it is impossible to put a dollar value on indemnities for disclosure in the government's financial statements, a description of some of the major categories of indemnities be included in the note to the financial statements that discloses indemnities.*

Response of the Ministry of Finance and Corporate Relations

The most important question surrounding guarantees and indemnities is whether the government is taking excessive risks, and acting irresponsibly. The Auditor General's report has essentially affirmed that no abuses are occurring.

The Auditor General's report identifies areas where the government could improve its policies and practices. We respond to the specific Auditor General recommendations below, in the same order in which they are identified in the report.

- *The Auditor General has identified that most ministries which do not routinely issue guarantees do not have procedures established for review, control and approval of guarantees. While we are not prepared to require that ministries develop detailed procedures to meet a situation which may never occur, ministries will be asked to ensure that their manuals at least note that guarantees have specific approval processes to be followed and who should be contacted for that information.*
- *The Auditor General has recommended that when risk assessments for individual guarantee requests under a program are the same and the ministry wishes to avoid repeating the same risk assessment, the ministry should get Treasury Board approval for the general assessment and the authority to not include assessments in the individual requests. We intend to adopt this recommendation.*
- *We intend to expand our policy to say that the source of standard agreements used in guarantee programs must be documented by the ministry responsible for that program.*
- *In accordance with the Auditor General's recommendations, the Ministry of Agriculture, Fisheries and Food is putting forward a Treasury Board submission seeking clear limits of delegated authority.*
- *Loans Administration Branch has already implemented the Auditor General's recommendation that consistent procedures be adopted for documenting the results of its investigations prior to paying out any guarantee claims.*
- *We will be reviewing whether the policy requiring that a central list be maintained of outstanding guarantees given by ministries and government corporations on an ongoing basis would serve a useful purpose. The results of that review will determine whether we recommend compliance or elimination of this requirement.*
- *The Office of the Comptroller General is currently reviewing the contents of the annual guarantees and indemnities report. This review may result in a change in the contents and an appropriate change in the* Financial Administration Act *(Act).*
- *The Auditor General has recommended that we include additional information on guarantees*

in the Public Accounts, in accordance with a pronouncement of the Canadian Institute of Chartered Accountants. The Office of the Comptroller General will consider this.

- *There appears to be a lack of knowledge of indemnities on the part of government financial officers. We are considering issuing an information booklet for government financial officers about indemnities and the associated government rules.*
- *The Auditor General has recommended that government corporations be required to maintain a list of all indemnities issued, which could be reconciled to the Risk Management Branch indemnity list. Most government corporation indemnities must be processed through Risk Management Branch before being approved. If a record of the indemnity resides with Risk Management Branch, there is no need for government corporations to maintain a duplicate list, although they will need a list of current indemnities.*

  We agree that government corporations allowed to approve their own indemnities should maintain a list of the indemnities they have issued and are outstanding. Therefore we intend to recommend a change to the policy to require government corporations which are authorized to approve their own indemnities to maintain a list of the outstanding indemnities they have issued.
- *We intend to modify the indemnities policy to be consistent with the Guarantees and Indemnities Regulation.*
- *As Risk Management Branch maintains a list of indemnities and expiry dates, we see no need to maintain duplicate records in each ministry. For indemnities with no expiry date the ministries should maintain a list of current indemnities.*
- *The Act requires that the Minister of Finance provide a list of indemnities issued and approved by the Treasury Board or the Lieutenant Governor in Council each fiscal year. The government has exceeded this requirement by including all indemnities issued by the Consolidated Revenue Fund. The Office of the Comptroller General is currently reviewing the contents of the report. This review may result in a change in the contents and an appropriate change in the Act.*
- *The Office of the Comptroller General is considering the possibility of expanding the description of indemnities outstanding in the Public Accounts.*

Land Tax Deferment Act

Land Tax Deferment Act

The* Land Tax Deferment Act *enables eligible property owners to defer payment of their property tax. The tax is paid to municipalities on their behalf by the government, and the full amount, plus interest, is repayable when the house is sold.

Audit Report

Audit Scope

We have made an examination to determine whether the *Land Tax Deferment Act* was being complied with, in all significant respects, as of November 1994. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

Audit Opinion

In our opinion, the *Land Tax Deferment Act* was being complied with, in all significant respects, as of November 1994.

Introduction

The *Land Tax Deferment Act* was enacted in 1974 to allow eligible persons to defer some or all of the property taxes payable on their principal residence. Through the property tax deferment program, the government pays the property tax on behalf of the owner, and registers a lien on the property as security for the tax and accumulating interest. Simple interest accrues at a rate which is set twice a year by regulation, and which must not exceed the prime rate of the government's banker, less 2%. For the period from October 1994 to March 1995, the rate was 5.25%.

While repayment of some or all of the accumulated deferred taxes and interest may be made at any time, the full amount remaining outstanding becomes payable when the property is sold or transferred, except if the property is transferred to one spouse on the death of the other. In addition, the minister may demand payment if circumstances arise such that the minister considers that the taxes and interest owing are inadequately secured by the equity in the property.

The Act is administered by the Land Tax Deferment Section of the Real Property Taxation Branch, under the authority of the Surveyor of Taxes in the Ministry of Finance and Corporate Relations.

Exhibit 4.1

Eligibility Criteria

Eligibility for deferring property tax is defined by the following criteria:

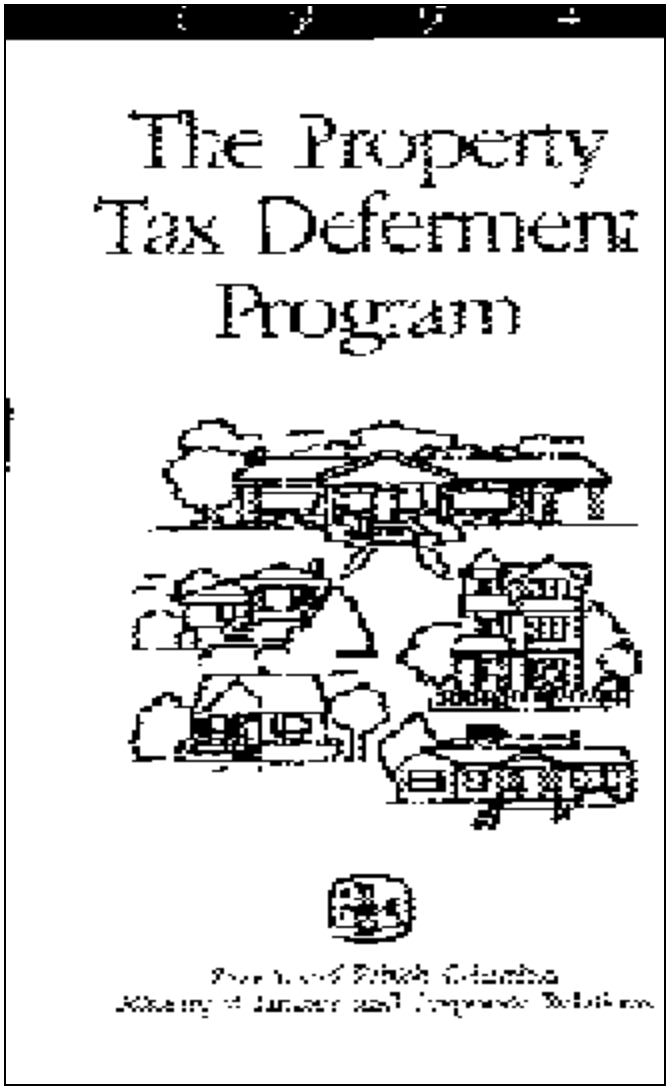
- the applicant must own the property (may be joint ownership);
- the property must include a building or manufactured home that is the applicant's principal place of residence;
- the applicant must have been ordinarily resident in British Columbia for at least the preceding year;
- the applicant must be a Canadian citizen or permanent resident;
- the applicant must be either age 60 years or older by the end of the year (prior to 1989, the requirement was 65 or older); or a surviving spouse who has not remarried; or handicapped, as defined by the *Guaranteed Available Income for Need Act;*
- where the property is owned by joint tenants or tenants in common, the "principal supporter" of the family must be eligible;
- the property taxes must not be more than six months in arrears;
- there must be sufficient equity in the property to secure the deferred taxes plus interest – policy requires that there be at least 25% equity in the property; and
- the application must be made prior to December 31 of the year for which taxes are to be deferred.

To be eligible for this deferral, an applicant must first meet all of the requirements outlined in Exhibit 4.1. The applicant fills out a form, and gives it to the taxing authority where the taxes would be paid. The taxing authority enters further information from the tax roll onto the application, certifies that taxes are not in arrears, and forwards the application to the ministry. The ministry then performs certain checks on eligibility and, if the results are satisfactory, draws up an agreement for the applicant to sign. Once received back by the ministry, the signed agreement is registered as a charge on the land title, and payment is made by the ministry to the taxing authority.

Deferral in subsequent years is not automatic. Each person must complete an annual renewal form (which is sent out every spring, together with a statement of the accumulated taxes and interest owing) and forward it to the taxing authority, which in turn forwards it to the ministry.

Most people defer the full amount of the taxes, but a lesser amount can be deferred, and it is not necessary to defer each year. In addition, full or partial repayment can be made at any time.

The agreement terminates and full repayment is required when the property is sold or transferred (unless it is transferred to a surviving spouse), or if the minister considers that the equity in the property is insufficient security for the cumulative amount of taxes and interest deferred. However, the agreement does not terminate simply because the applicant ceases


The Property Tax Deferment Program

Public information brochure about the program

to be eligible. For example, someone who was eligible because she was widowed would cease to be eligible when she remarried (assuming that she was not also over 60 years old or handicapped), and so could not defer taxes in the future. However, the previously deferred taxes would only have to be repaid if the property was sold or transferred, or if the equity became insufficient.

As of September 1994, approximately 7,200 people had

deferred their property taxes, and the total amount of the deferred taxes and interest exceeded $58 million. The majority of people who defer their taxes are over 60 years old, but the government has estimated that less than 2% of eligible people over 60 have deferred their taxes.

Audit Scope

Our audit was conducted to determine whether the *Land Tax Deferment Act* has been complied with, in all significant respects, as of November 1994. We looked at both the eligibility criteria and the various administrative aspects of the legislation. We did not limit our audit to reviewing the government's procedures for assessing compliance; rather, where we felt it appropriate, we extended our tests to determine for ourselves whether the Act was being complied with. In the course of our work, we met with ministry staff and reviewed applications for tax deferrals, as well as checking with information from other sources where necessary.

We did not audit certain sections of the Act that deal specifically with 1974 property taxes. These sections established different criteria that allowed applications from any property owner, thus including persons who would not have qualified under the main eligibility criteria. These different criteria applied only for 1974. They allowed anyone whose property taxes for 1974 had increased by more than 20% from 1973 to apply for deferral, but the maximum amount that could be deferred was the amount of the increase that exceeded 20%. As well, there was a legislated repayment schedule. All of the agreements that were entered into under these criteria have been paid out, and so these sections of the Act are effectively spent.

In addition, the ministry no longer requires that applicants be the principal supporter of the family, and so we did not audit for compliance with this requirement of the Act either.

Our tests were carried out on a sample of 320 files: 20 new applications for 1994 and 300 agreements that were made in prior years. We carried out some tests, such as verifying the amounts paid to the municipalities, on a smaller sample. Our work was performed in November and December 1994.

Overall Observations

We found that:

- apart from some minor exceptions, the applicants were eligible;
- the administrative parts of the Act – such as the approval of the deferral agreement, the registering of the charge against the land title, making the payment to the municipality, correctly calculating the interest, and properly discharging the agreement when it is paid off – were being complied with; and
- apart from some minor exceptions, the existing agreement holders remain eligible to defer their current taxes, and no deferred taxes should be repaid due to sale of the property or equity becoming insufficient.

Audit Findings

Eligibility at the time of application

For our sample of 320, we attempted to verify that, when the application was made:

- the applicant was eligible because she or he was over 60 (or 65 if the application was before 1989), or handicapped, or was a surviving spouse who had not remarried;
- the applicant owned the property;
- the applicant had lived in British Columbia for at least the previous year;
- the applicant was a Canadian citizen or permanent resident;
- the property was the principal residence of the applicant; and
- there was sufficient equity in the property.

Of our sample, 287 people were eligible because of their age, 6 were handicapped, and 27 were surviving spouses who had not remarried.

We were able to verify that all of those who were handicapped or a surviving spouse, were eligible. We were also able to verify the ages of 281 of the 287 who were over 60 (or 65 if they applied prior to 1989). We were unable to verify the ages of the other 6. However, given the individual circumstances and the nature of the records that we could inspect, we were not concerned that we could not independently verify their ages. Two people, we noted, had given incorrect ages on their applications, and had thus deferred their taxes one year before being eligible.

We were also able to verify that all of the applicants owned the property for which they were applying, all except four had lived in the Province for the prior year and, for all except nine, the property was their principal residence. We could not prove to our satisfaction that those 13 were eligible, but nothing came to our attention to suggest that they were not.

All applicants to defer property taxes sign a form which indicates that they are either Canadian citizens or landed immigrants. We were able to independently verify that the majority of our sample were Canadian citizens.

An additional procedure performed by the ministry is to check the names of new applicants against the database of existing agreements to ensure that no one is deferring taxes on more than one property. We reviewed the work of the ministry in this area and found that the duplicate names reported by the system were satisfactorily cleared.

By policy, the ministry requires that all applicants have a minimum of 25% equity in their property (prior to 1989, this was 20%). The Act defines the market value of the property as the assessed value, and this is compared to the amount of any mortgages registered against the land title plus the amount of the deferred taxes. The ministry obtains a copy of the mortgage document from the Land Titles

Office. If the amount of the mortgage on the document registered at Land Titles results in the equity being less than 25%, or if the mortgage is of the type that increases (sometimes called a reverse mortgage), the ministry requests the applicant to provide information from the mortgagee as to the current amount outstanding, and recalculates the equity.

We found mortgages on the properties of 115 applications and, for all except 10, we were able to verify that the equity was satisfactory. For those 10, we were unable to obtain a copy of the mortgage agreement, which had since been cancelled. At the time of the application, all of which had been made before 1982, no copy of the agreement had been placed on file. We did not find any exceptions for the more recent applications.

In summary, out of our 320 audit samples, we found only 2 exceptions (age incorrect). Accordingly, we concluded that, as far as the eligibility of the applicants was concerned, the *Land Tax Deferment Act* was being complied with in all significant respects.

For a number of the samples, as described above, we could not independently verify that the applicant was eligible in all respects. Due to the inherent nature of the records used and the amount of time that had passed since the application had been made, we considered the extent of these shortcomings to be reasonable.

On only one main point are we concerned with compliance with eligibility. Although the ministry no longer requires that applicants be the principal supporter of the family, the legislation does. While we did not attempt to audit this section of the legislation, we believe, based on our review of the applications, that at least 12 applicants out of the 320 are not the principal supporter of the family, and the person who does appear to be the principal supporter (a spouse or adult child) is not eligible in his or her own right to defer the taxes.

In this respect, therefore, the Act is not being complied with.

We recommend that the ministry either obtain approval for an amendment to the Act to delete the requirement that the applicant be the principal supporter of the family, or take steps to ensure compliance with section 5(5)(b) of the Act.

Administration

We audited a number of administrative areas of the *Land Tax Deferment Act*:

- the application, whether it is the first application or a subsequent renewal, must be made prior to December 31 of the year for which taxes are to be deferred;
- the agreement must be signed by both the applicant and the ministry;
- the agreement must be registered against the land title;
- the correct amount must be paid to the municipality;
- the ministry must send out a statement each year, detailing the cumulative amount of taxes deferred and interest accrued; and

- when an agreement is paid out, the correct amount must be received and the charge removed from the land title.

Our tests were carried out on our sample of 320 files, except that the calculation of the balance of principal and interest was tested on a sub–sample of 60 files, and the payment to the municipality and the paying out of the agreement was tested on separate samples of 20 files each.

We found that all of the applications were made on time, and that there were signed agreements on all files. We also found that all of the agreements, except four, had either been registered against the land title or, where the property was owned by the Director of the *Veteran's Land Act*, that there was an agreement in place with the Director.

In one of the four cases in which the agreement was not registered, the Land Titles Office had written back to the ministry stating why it would not register the agreement. The ministry had then provided additional information. At that point, we believe, there was a breakdown both in communication with the Land Titles Office and in the ministry's own system, for we found that although the ministry thought that the agreement had been registered against the title, in fact it never was. This property has now been sold, as is discussed later in this report.

In the second case, the property for which the application was made was owned by the Director of the *Veteran's Land Act*, and thus the agreement was not registered against the land title at that time. Under this Act, veterans are assisted in the purchase of a property. Until a veteran has paid off the loan, title to the property rests with the Director of the *Veteran's Land Act*. In effect, the property is owned by the Crown and no charge can be registered against the title. In these situations, the agreement to defer the taxes is signed by the Province, the taxpayer, and the Director. When the loan is paid off and the property is transferred to the veteran, the ministry is supposed to be informed, in accordance with the agreement, so that it can then register the tax deferment agreement against the land title. In this particular instance, however, we found that the ministry had not been told of the transfer of ownership, and so the agreement was not registered.

In the third case, the agreement was not showing on the land title, even though the ministry had received back from the Land Titles Office a copy of the agreement with that Office's stamp of registration on it. In the fourth case, the agreement was shown as pending on the land title, even though it had been sent in one year earlier.

For all of these cases but one – the property that had been sold – the agreement for the deferral of taxes had been properly registered.

On the matter of correct payment to the municipality, we found that this requirement was met in 1994.

We also found in our sample that a statement was sent out in 1994 to the agreement holders, and the cumulative balance of deferred taxes and accrued interest shown on each statement was correct.

From our sample of agreements that had been paid out, we noted that the correct amount had been received (interest is calculated up to the day that the payment is received) and the charge had been promptly removed from the land title.

Accordingly, we concluded that, with respect to these administrative activities, the *Land Tax Deferment Act* was being complied with in all significant respects.

Continuing Eligibility

As well as verifying that the applicants were eligible at the time that the application was made, we also wanted to verify that the applicants were still eligible to defer the current taxes, or that the agreement should not have been repaid.

For the 300 agreements in our audit sample that had been entered into before 1994, we set out to verify that:

- the property was still owned by the applicant;
- the property was still the principal residence of the applicant;
- the equity was still above the minimum set by policy; and
- the taxes were not in arrears (if the applicant had not been deferring each year).

If any one of the above conditions does not hold true for an agreement, then there should be no current deferral of the property taxes. In addition, if the property has been sold or if the taxes are in arrears, then the agreement should be terminated and the balance repaid. If the equity is below the minimum, then the minister may terminate the agreement.

In all cases except one, we found that the applicant or surviving spouse was still a registered owner of the property. In the one exception, the agreement had not been registered against the property (as noted above under "Administration"), and the property had been sold in 1992. The application to defer taxes was made in 1990, the only year in which taxes had been deferred. There had been no deferral of taxes after the property was sold, but the amount deferred should have been repaid when the property was sold. The amount of the taxes and interest owing as of November 1994 was $1,520. This the ministry is attempting to recover.

Apart from the property noted above which had been sold, we found four agreements in which it appeared that the property was no longer the principal residence. For three of these agreements, the property taxes in the current year are not being deferred and the agreement holders are still registered owners of the properties. Thus, there is no conflict with the legislation.

For the other agreement, however, the current taxes are being deferred, although it appears that the owner of the property has

been living in an intermediate care home since 1993 (the property is not, apparently, being rented out during this time). Strictly, this person should not be deferring the property taxes while living elsewhere, but we consider that this situation calls for some flexibility since there is the possibility of the owner returning home.

We compared the current assessed values of the properties with the maximum possible amount of the mortgages recorded against the land title, updated for the current year where the mortgage was a reverse mortgage, plus the current cumulative amount of taxes deferred and interest accrued. We found that the equity on all of the properties was more than 25%.

We also looked at 22 files in our sample in which mortgages had been taken out since the agreement for the deferral of taxes was registered against the title. The impact of these mortgages on the requirement for 25% equity is not a concern since the tax deferment agreement would have priority over these mortgages. However, we still wanted to see to what extent the equity might be reduced. In three cases, we found it was reduced below 25%; in one case, the equity when the new mortgage was taken out was reduced to 6%. The mortgagees were all recognized financial institutions, and we believe that if they consider that there is sufficient security for their mortgage, which ranks after the tax deferment agreement, then there is no concern for the security of the taxes deferred.

When an agreement holder applies to defer the property taxes for the current year, the municipality must certify that the taxes on that property are not in arrears. We found that approximately 12% of the agreement holders had not applied to defer their 1994 property taxes at the time of our audit in November 1994. We took a sample of approximately 30% of these and verified with the appropriate municipality that their taxes were not in arrears.

Out of our 300 samples, we found only 2 exceptions: the property that had been sold, and the person deferring the taxes while not living at the property.

Other Observations

During the course of our audit, a number of other matters not directly related to compliance with the Act came to our attention. These were mainly in the areas of interest rates and legislation.

Rate of Interest

We have estimated that setting an upper limit to the interest rate of the prime rate of the government's banker, less 2%, means that the outstanding balance of almost $49 million of deferred taxes receivable (excluding accumulated interest) will cost the government approximately $2 million in the fiscal year ended March 31, 1995.

We arrived at this figure by comparing the actual rate charged on the deferred taxes – 3.5% for April 1, 1994 to September 30, 1994, and 5.25% for October 1, 1994 to

March 31, 1995 – to the concessionary loan rate for the same period – 9.19% – and applying the difference to the average balance of principal outstanding for the same period. The concessionary loan rate is a blend of the rate the Province would have to pay if it were to borrow money for a 5–, 10– or 20–year term — a similar time frame for which the deferred taxes might be outstanding. This rate was provided to us by the Debt Management Branch of the Ministry of Finance and Corporate Relations.

While the Legislature saw fit to include this limit on the interest rate, we do not think that this benefit to the property taxpayer is consistent with the rest of the legislation, which does not impose any eligibility qualification as to income. The government's independent financial review conducted in 1991 recommended that "this limit on interest for land tax deferment be reconsidered to ensure it is not used as an inexpensive borrowing source. The rate should be at least equal to, and preferably slightly higher than, the current available investment yield on short–term funds."

We recommend that the current interest rate requirement of not more than the government banker's prime rate, less 2%, be reconsidered and possibly raised to equal that which the government otherwise obtains on its short–term investment funds.

In considering whether raising the interest rate might be a financial burden on the property owner, we calculated, for the agreements in our sample that were taken out prior to 1990, the average annual increase in the assessed value of the property over the life of the agreement. For the same properties, we also calculated the average annual increase in the assessed value, net of the balance of taxes deferred. We found that the average annual increase in the assessed value of the property was a little over 11%, and that deferring the taxes had the effect of reducing this average annual increase in equity by about 0.7%.

In addition, we found that the method of setting the rate of interest can mean that the rate charged, even though it is low, may be very different from the government borrowing rate in times when the rate is fluctuating. The Act requires that the rate be set semi–annually, in advance, and be based upon the rate of the government's banker on the 15th day of the 4th prior month. For example, the rate of 5.25% that was in effect from October 1, 1994, to March 31, 1995, during which time our audit was performed, is based on the rate in effect on June 15, 1994.

To keep the interest rate on land tax deferment more current, we recommend that consideration be given to amending the legislation so that the rate is set at the end of every three months, based on the rate at the end of the previous month.

The Legislation

We found that the Act does not cover all situations that arise in land tax deferment, and that, as a result, the ministry has had to develop its own practices in dealing with these situations.

For example, the Act as written does not allow tax to be deferred on property held in trust or held by an executor. However, ministry practice is to allow deferral in these situations, provided that the person for whom the property is held in trust, or who is to be the beneficiary of the estate, would be eligible to defer the taxes. Nowhere, however, is this practice written down.

The ministry has already made a review of the legislation, identifying these and other issues of concern.

We recommend that consideration be given to reviewing and updating the Land Tax Deferment Act *for matters identified by the ministry and this audit.*

Summary of Recommendations

The Office of the Auditor General recommends, that:

- *The ministry either obtain approval for an amendment to the Act to delete the requirement that the applicant be the principal supporter of the family, or take steps to ensure compliance with section 5(5)(b) of the Act.*
- *The current interest rate requirement of not more than the government banker's prime rate, less 2%, be reconsidered and possibly raised to equal that which the government otherwise obtains on its short–term investment funds.*
- *To keep the interest rate on land tax deferment more current, consideration be given to amending the legislation so that the rate is set at the end of every three months, based on the rate at the end of the previous month.*
- *Consideration be given to reviewing and updating the* Land Tax Deferment Act *for matters identified by the ministry and this audit.*

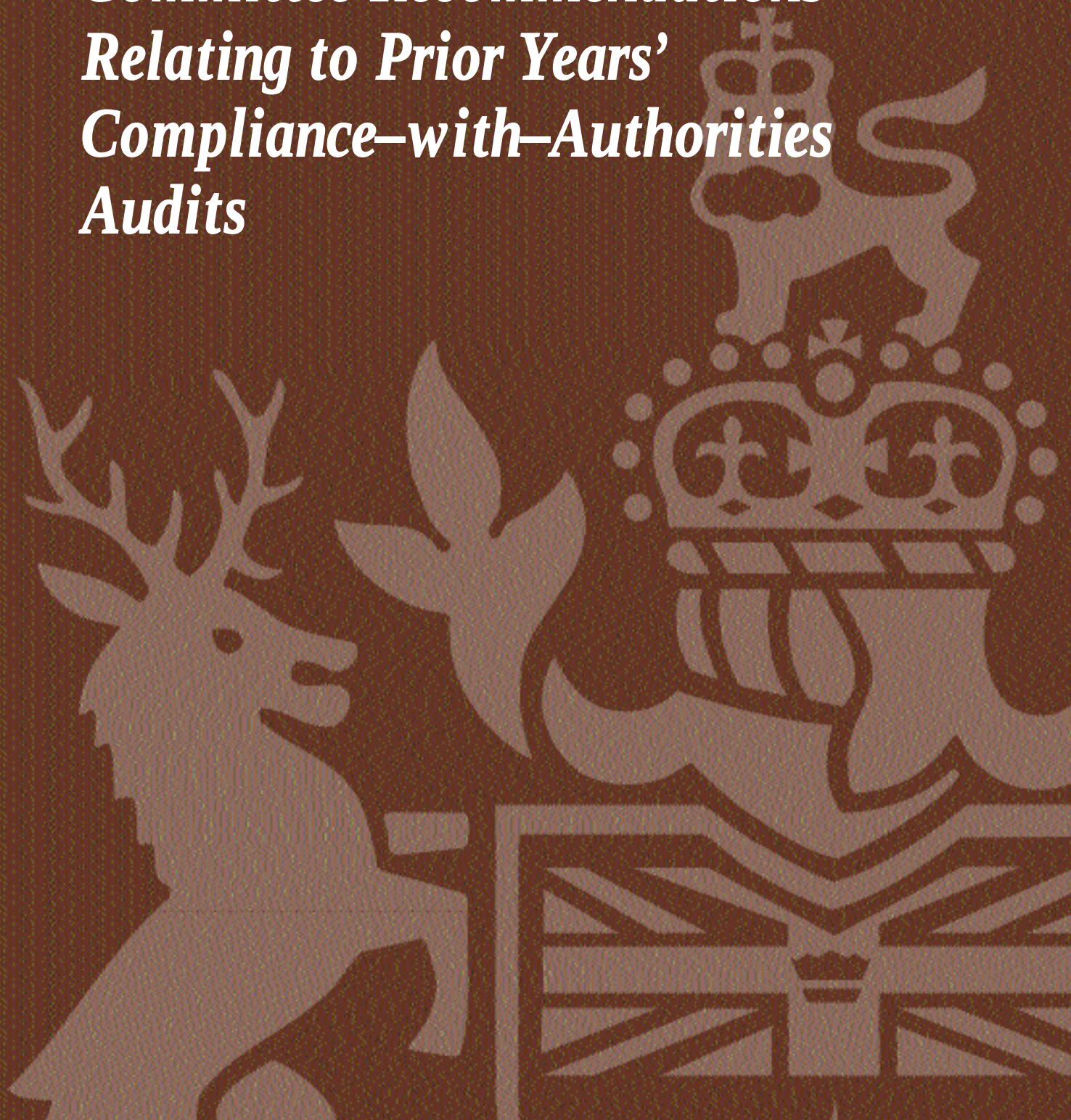
Response of the Ministry of Finance and Corporate Relations

The Ministry regards its role as being to administer the Land Tax Deferment Act *in ways which are effective and practical within the overall mandate of the statute.*

Many years ago, the requirement that the applicant be the "principal supporter" of the family, was administratively deleted from the eligibility requirements, as it was both cumbersome to monitor, and onerous to tax deferment applicants. While correctly intentioned to target tax assistance to the owner supporting the household expenses, the principal supporter eligibility requirement would have involved receiving and analyzing annual income and/or financial statements of all household members, fostering a negative income test environment, for very little additional control over the program.

The ministry supports the recommended amendment to the Act, to remove the "principal supporter" eligibility requirement. The recommended amendments to the Act regarding the deferment interest rate and frequency of rate adjustment, and for describing deferment situations not anticipated when the statute was drafted in 1974, will be reviewed for future consideration by the provincial Cabinet.

Status of Public Accounts Committee Recommendations Relating to Prior Years' Compliance–with–Authorities Audits



Status of Public Accounts Committee Recommendations Relating to Prior Years' Compliance–with–Authorities Audits

In each of our audits we make suggestions and recommendations, some of which are subsequently endorsed by the Select Standing Committee on Public Accounts and adopted as recommendations for its reports to the Legislative Assembly.

In March 1995 we obtained from ministries, for publication, updated responses to the recommendations of the Select Standing Committee on Public Accounts, relating to our prior years' audits.

The following section includes the Committee's recommendations, the ministries' responses, and our comments thereon for the following prior years' audits:

- Statutory Tabling Requirements
- Safeguarding Moveable Physical Assets
- Treatment of Unclaimed Money
- Compliance with the *Financial Disclosure Act*
- Order–in–Council Appointments
- Compliance with Part 3 of the *Financial Administration Act*
- *Financial Information Act*: Follow–up
- Compliance with Part 4 of the *Financial Administration Act* and its Related Regulations
- Compliance with the *Financial Information Act*, Regulation, and Directive

Committee recommendations that the ministries state have been implemented or otherwise resolved, are not repeated in our subsequent year's report.

Statutory Tabling Requirements
(Auditor General 1993/94 Report 4, May 1994)

Recommendations of the Select Standing Committee on Public Accounts, July 1994 Report

Your Committee recommends that the recommendations contained in the Auditor General's Report 4 respecting statutory tabling requirements be implemented by the government. However, consideration should be given to varying the standard content or timing requirements for particular organizations where circumstances may warrant.

The Auditor General's Recommendations:

General

We recommend that consideration be given to having all tabling requirements consolidated into one Act which, along with supporting regulations or policies:

- identifies the organizations required to table reports;
- specifies the content requirements of the reports;
- clarifies the meaning of terms used in tabling requirements;
- specifies the timing requirements for tabling reports;
- includes a requirement for monitoring whether reports are tabled on time and for reporting these facts, along with explanations, to the Legislative Assembly; and
- provides for an alternative method of releasing reports when the House is not in session.

Clarity of Requirements

We recommend that the terms used to describe the time requirements for tabling reports be defined clearly. This could be achieved either by defining the terms in each Act that has tabling requirements, or by defining them in one central Act, such as the *Interpretation Act*, or in a new Act containing tabling requirements for all organizations required to table reports.

Consistency of Requirements

We recommend that all ministries and organizations included in the government's summary reporting entity be required to table their annual reports. Exceptions could be made for organizations that are inactive. However, the inactive organizations should still be required to table financial statements each year, along with an accompanying explanation.

We recommend that the length of time within which annual reports must be tabled be consistent for all organizations, including government ministries. One way this could be achieved

would be to have one Act that specifies the tabling requirements for all government and related entities.

We recommend that the legislation requiring a report to be tabled include more specific guidance about the content of the report, or that it be supplemented by policies specifying content requirements.

Monitoring

We recommend that a member of Cabinet, possibly the Minister of Finance and Corporate Relations, as Chair of Treasury Board, be given the responsibility for producing a report for the House listing all reports which should have been tabled in the previous session. The report should include the dates that reports have been tabled, compared to the dates that they were required to be tabled, the name of the Ministry responsible, and any explanation for reports not tabled on time. Such a report should itself be timely. To do this, it could be submitted to the Clerk of the House and made public within 30 days of the session being adjourned; then tabled when the Legislature next sits.

If our previous recommendation to have all tabling requirements included in one Act is followed, then the Minister responsible for that Act should produce this report.

Timeliness of Making the Information Available to the Public

We recommend that all organizations be required to table their annual reports within three months of their year–end if the House is in session.

We recommend that the statutory provisions for the tabling of documents be revised to include a provision for filing the reports with the Clerk of the House and releasing them to the public when the House is not in session. The copy given to the Clerk would become the “official copy” and would be tabled as soon as the House next sits.

Inactive, Wound up, or Reorganized Entities

We recommend that, where a government organization has merged with another organization, its enabling statute be amended to delete the reporting requirement. Where an organization has been dissolved, the enabling legislation should be repealed.

We recommend that, when ministries are disestablished or reorganized, the orders in council authorizing and describing the transfer of responsibilities also clarify the reporting requirements of the new or remaining ministries. In addition, consideration should be given to repealing the enabling statutes for the disestablished ministries.

Commissions of Inquiry

We recommend that the Ministry of Attorney General, which is responsible for the *Inquiry Act*, ensure that the requirement for the tabling of the commissioners' reports in the Legislative Assembly is communicated to the Minister who is responsible for the commission at the time of each commissioner's appointment.

Regulations

We recommend that the Acts requiring the tabling of regulations in the Legislative Assembly be amended to remove these requirements.

Response of the Ministry of Attorney General

The Ministry currently provides a briefing package to incoming commissioners. The requirement to table a report in the Legislature will be added to the package as an interim measure. The method of communicating this requirement to the appropriate Minister is under review.

Response of the Ministry of Finance and Corporate Relations

The Ministry of Attorney General put forward an amendment to the Constitution Act *in 1993 that would have addressed a number of the issues raised by the Auditor General. This amendment died on the order paper. No further action has been taken or is planned on a government–wide basis.*

Comment by the Office of the Auditor General on the Responses of the Ministries

We are encouraged by the actions being taken with regard to Commissions of Inquiry. However, no action has been taken or is planned to address the several other Auditor General recommendations approved by the Public Accounts Committee.

Safeguarding Moveable Physical Assets

(Auditor General 1993/94 Report 4, May 1994)

Recommendations of the Select Standing Committee on Public Accounts, July 1994 Report

Your Committee recommends that the recommendations contained in the Auditor General's Report 4, relating to safeguarding moveable physical assets, be implemented to the extent that it is cost effective and efficient to do so.

The Auditor General's Recommendations:

Non–Compliance with Government Policies for Safeguarding Moveable Physical Assets

We recommend that the Office of the Comptroller General and the ministries should be monitoring how well they are complying with the policies for safeguarding moveable physical assets. Where they find that the level of compliance is inadequate, we recommend that they take appropriate steps to ensure that policies are followed. Where they find that policies are absent or incomplete, we recommend that they write or revise the required policies.

Clarity in Defining and Recording Assets

We recommend that the criteria used for all asset records be consistent, using a specific dollar amount which is updated periodically as required (for example, at the beginning of each fiscal year).

We recommend that ministry determinations of cost/benefit of control be evaluated and assessed by the Office of the Comptroller General before being accepted as a basis on which to dispense with the maintenance of physical asset records.

We recommend that, for physical assets which are common across government (such as computers, computer software, and furniture), the government policy manual give clear guidance on what to include as attractive assets and what to exclude, by listing specific examples. For physical assets that vary from ministry to ministry (such as equipment), each ministry should be required to provide specific guidance in their own manuals on what assets to record and control as attractive, including a list of those that are unique to the ministry.

We recommend that the government policy manual be clarified to indicate that an asset may be both fixed and attractive.

The manual should clearly state that, where a fixed asset also meets the criteria for attractive assets, the additional and more stringent requirements for safeguarding attractive assets must be complied with, not just the requirements for recording and controlling fixed assets.

Content of Asset Record Systems

We recommend that the following information requirements for asset records be considered for addition to the policy manuals:

- name of the custodian (for all assets, not just attractive assets);
- purchase information (including invoice and supplier number);
- description information (model number, manufacturer, and colour);
- the ministry–assigned, unique identifying number (the bar code or tag number);
- cost;
- estimated useful life; and
- warranty references.

Form of Asset Record Systems

We recommend that consistent and compatible physical asset recording systems be used throughout government, and especially within ministries.

Centralization of Asset Record Systems

We recommend that the government policy manuals establish criteria for physical asset record systems. This will ensure that sufficient commonality exists between systems to allow the exchange of data, whether the physical asset systems are centralized within ministries or within government.

Periodic Physical Counts

We recommend that bar code readers be made readily available to organizations to facilitate the counting of physical assets tagged with bar codes.

Items Incorrectly Recorded as Physical Assets

We recommend that policies be established to determine when it is appropriate to record professional fees as asset purchases, and when it is not.

Findings Related to Computer Equipment and Software

We recommend that the asset records show what components have been added to a computer, with the relevant serial number recorded to identify it.

We recommend that government policies be developed to address the purchase or use of government computer equipment for work at home.

Findings Related to Technical and Office Equipment

We recommend that, as a matter of policy, ministries be required to obtain a receipt from the lessor for the return of a leased item when a lease expires and is not renewed.

Findings Related to Furniture

We recommend that when furniture is purchased it be tagged with a unique number and, as a minimum, be recorded in a list of furniture for the particular branch office. Physical verification should be done where there have been changes to the location or a large number of disposals.

Findings Related to Vehicles

We recommend that government policy be amended so that a local manager can approve overnight home parking when it is appropriate for travel purposes.

Response of the Ministry of Finance and Corporate Relations

The Office of the Comptroller General will be reviewing financial management policy on asset management when resources permit.

Comment by the Office of the Auditor General on the Response of the Ministry

No progress has been made to date to implement the Auditor General recommendations approved by the Public Accounts Committee.

Treatment of Unclaimed Money

(Auditor General 1993/94 Report 4, May 1994)

Recommendations of the Select Standing Committee on Public Accounts, July 1994 Report

Your Committee recommends that the recommendations contained in the report "Treatment of Unclaimed Money" be adopted and implemented.

The Auditor General's Recommendations:

Money Deposited in the Treasury of the Province

We recommend that a limit such as $100 be set so that deposits below this benchmark can be transferred to revenue by the government after a much shorter period of time than 10 years (such as five years). This would not extinguish the right of a valid claim on these amounts, but would remove them earlier from the active accounting records to the statement of unclaimed money. Alternatively, consideration could be given to transferring smaller amounts early, and extinguishing rights to claiming them at the time they are transferred, to avoid the costs of maintaining the records.

Money Received by Companies or Persons

We recommend that a comprehensive study be initiated to review all types of unclaimed money and other types of unclaimed assets held by companies or persons within the Province, other than those to which the *Bank Act* (Canada) applies. The study should determine an appropriate up–to–date manner for handling and accounting for such money and assets, addressing provisions for monitoring, enforcement, and full public disclosure. This may require amendment of existing legislation or implementation of new legislation.

Other Provincial Statutes Directly Related to the Unclaimed Money Act

We recommend that the sections of these provincial statutes be included in the scope of any study of unclaimed money and other assets held in the Province as we recommended above, which should consider among other issues the appropriate monitoring, enforcement, and disclosure requirements.

Information to the Public

We recommend that the government provide a public advertisement in newspapers stating when and where information about unclaimed money is available. This should be done periodically, as well as at the time at which the information becomes available each year. It

should be an important consideration in any future amendment to the *Unclaimed Money Act* and related legislation.

Payment of Claims

We recommend that the government consider reinstituting periodic search procedures for persons or companies who may be rightfully entitled to unclaimed money deposits that have been transferred to the government's Consolidated Revenue Fund.

We recommend that the legislation be amended to require the inclusion of the successful claims that were paid out in the statement of unclaimed money so that it becomes a complete record of outstanding unclaimed money.

Responsibility for the Unclaimed Money Act

We recommend that the Ministry of Finance and Corporate Relations identify which Ministry branch is responsible for administering the *Unclaimed Money Act* in its annual report.

Response of the Ministry of Finance and Corporate Relations

The Office of the Comptroller General has formed a study group to review how unclaimed money is currently administered within the Province and in other relevant jurisdictions. This review is in progress. The study group will make recommendations based on its findings.

Comment by the Office of the Auditor General on the Response of the Ministry

We are encouraged by the actions being taken to address the Auditor General recommendations approved by the Public Accounts Committee.

Compliance with the Financial Disclosure Act

(Auditor General 1993 Annual Report, March 1993)

Recommendations of the Select Standing Committee on Public Accounts, July 1993 Report

Your Committee recommends:

a) that the Financial Disclosure Act *be amended as follows:*

i) to clarify who is responsible for enforcing the Act,

ii) to bring the Islands Trust, and related local trust committees, within the purview of the Act,

iii) to require a different frequency of filing of disclosure, such as annually; when there is a material change to report; or some combination of these or other alternatives;

b) that the Financial Disclosure Act *Forms Regulation be amended:*

i) to specify the length of time disclosure forms should be retained,

ii) to allow for flexibility in the style of disclosure forms, so long as the required content and approval aspects are consistently retained,

iii) so that the forms clearly specify the information that should be included,

iv) to provide greater certainty to someone inspecting the forms that a "nil" return is indeed correct.

Response of the Ministry of Attorney General

a) That the Financial Disclosure Act *be amended*

i) Ministry of Attorney General, Policy and Legislation is responsible for the Act. The Act is enforced by means of an offence section which provides for a maximum fine of $10,000 for those who fail to file a disclosure under the Act. The legislation is thus enforced by the Courts. Attorney General staff intend to prepare an informal guide to disclosure, laying out requirements in plain language. It is planned that the guide will be distributed to school districts, municipalities, and regional districts by the fall of 1995.

ii) The Ministry of Municipal Affairs is currently considering whether the Islands Trust should be included in the Act. A decision is expected in the fall as to whether this would form part of the 1996 legislative agenda.

iii) Amendments to the Act are now being considered to reduce the annual filing requirements from two to one.

b) That the Financial Disclosure Act *Forms Regulation be amended*

i) This is awaiting the recommendation of a UBCM analyst who is conducting a review of this matter.

ii) No action taken since last response.

iii) No action taken since last response.

iv) No action taken since last response.

(The last response indicated that representatives from three ministries (Attorney General, Education, and Municipal Affairs) had met to discuss the recommendations and had undertaken a number of tasks to deal with the recommendations.)

Response of the Ministry of Municipal Affairs

The Ministry of Municipal Affairs is now in a position to support the inclusion of the Islands Trust within the purview of the Financial Disclosure Act. We are advising the Ministry of Attorney General of our support for the preparation of such an amendment.

Comment by the Office of the Auditor General on the Responses of the Ministries

The first recommendation (a)i)) is resolved. We are encouraged by the actions being taken to address the other recommendations related to the Act. However, very little progress seems to have been made on the recommendations related to the regulation.

Order–in–Council Appointments

(Auditor General 1993 Annual Report, March 1993)

Recommendations of the Select Standing Committee on Public Accounts, July 1993 Report

Your Committee recommends:

a) *that requirements for the authorization of remuneration, particularly the application of the* Interpretation Act *where more specific legislation is silent, should be communicated to all parties involved in the appointment process;*

b) *that appointing Orders–in–Council clearly refer to remuneration, if any has been authorized (this may be done either by specifying the remuneration in the Order in Council, or by stating where the remuneration is authorized);*

c) *that the* College and Institute Act *and the* Insurance Corporation Act *be amended so that the authorization of remuneration for their appointees is consistent with the requirements for appointees to other government organizations;*

d) *that the term "Crown Corporation", which is used in Treasury Board guidelines relating to levels of remuneration for Order–In–Council appointees, be clearly defined.*

Response of the Ministry of Attorney General

a) *A Guide to the Cabinet Committee System has been issued by the Cabinet Planning Secretariat and distributed to parties involved in the appointment process.*

b) *Part 7 of the Guide to the Cabinet Committee System dated December 1993 and January 1995, states that, "Appointment Orders in general require remuneration to be stipulated in the OIC".*

c) *Effective February 15, 1995, legislation has been passed modifying the appointment process under the* College and Institute Act *to be consistent with the requirements for appointees to other government organizations.*

Response of the Ministry of Finance and Corporate Relations

The term (Crown Corporation) has been clarified to have the same meaning as government corporation, as defined in the Financial Administration Act. *This clarification will be included in the next update to the Government Policy Summary.*

Response of the Ministry of Skills, Training and Labour

Please be advised that in the Spring 1994 Legislative Session, the College and Institute Act *was amended to provide that the Lieutenant Governor in Council may set the remuneration that an institution pays to members of its board (section 10(1)). This amendment was brought into force on January 15, 1995. Order–in–Council 0180/95 sets the amount of remuneration that may be paid to members appointed to the boards of colleges, university colleges and institutes as well as to student members elected to the boards. It also sets the amount of remuneration payable to board Chairs.*

Response of the Ministry of Transportation and Highways

We wish to advise that the matter (amendment of the Insurance Corporation Act*) has not yet been resolved by government, however, we will continue to ensure, in the future, that government direction is secured. Hopefully, this matter can be resolved within a reasonable period of time.*

Comment by the Office of the Auditor General on the Responses of the Ministries

Based on the four ministries' responses above, it would appear that all of the recommendations have been satisfactorily addressed, except for the recommended amendment to the *Insurance Corporation Act*.

Compliance with Part 3 of the *Financial Administration Act*

(Auditor General 1993 Annual Report, March 1993)

Recommendations of the Select Standing Committee on Public Accounts, July 1993 Report

Your Committee recommends:

- *that the* Financial Administration Act *be amended to require all government write–offs, extinguishments and remissions to be reported together in one statement in the government's financial statements, whether authorized by the Act or by any other authority; and*
- *that the* Offence Act *be amended to create specific legislative authority for the Lieutenant Governor in Council to enact regulations to charge interest on overdue fines.*

Response of the Ministry of Finance and Corporation Relations

The Financial Administration Amendment Act*, passed in the 1994 spring legislation session, and effective April 1, 1995, requires all government writeoffs, extinguishments and remissions to be reported regardless of the authorizing statute. Authority to charge interest on overdue fines would require an amendment to the* Offence Act. *This change has been proposed by the Ministry of Transportation and Highways for the upcoming legislative session.*

Comment by the Office of the Auditor General on the Response of the Ministry

The first recommendation is resolved, and we are encouraged by the action being taken to address the other recommendation to amend the *Offence Act*.

Financial Information Act: Follow–Up

(Auditor General 1993 Annual Report, March 1993)

Recommendations of the Select Standing Committee on Public Accounts, July 1993 Report

Your Committee recommends:

a) that consideration be given to amending the regulation so that remuneration information for all publicly elected and appointed officials be disclosed regardless of how much they are paid;

b) that clearer guidelines be defined for

i) the types of expenses which should be disclosed as employee expenses

ii) which organization the Act applied to

iii) the treatment of severance agreement information;

c) that approval of all schedules be included in the Statements of Financial Information;

d) that consideration be given to amending the Act to require the inclusion of a statement of management responsibility in the Statements of Financial Information;

e) that requirements regarding availability of the financial information periodically be re–emphasized to both the public and the staff at the preparer organizations, by the Office of the Comptroller General and the responsible Ministries.

Response of the Ministry of Finance and Corporate Relations

Action has been taken on all of the recommendations.

Comment by the Office of the Auditor General on the Response of the Ministry

We are pleased that all of the recommendations have been implemented.

Compliance With Part 4 of the *Financial Administration Act* and Its Related Regulations

(Auditor General 1992 Annual Report, June 1992)

Recommendations of the Select Standing Committee on Public Accounts, July 1993 Report

Your Committee recommends:

- *that the Minister of Finance and Corporate Relations conduct a review of the interpretation and application of section 21 (i.e. special warrants) of the* Financial Administration Act *and present amendments to the Legislative Assembly that will address the concerns expressed by the Auditor General in his June 1992 Annual Report.*

Response of the Ministry of Finance and Corporate Relations

No comment.

Comment by the Office of the Auditor General on the Response of the Ministry

No progress seems to have been made to address the recommendations.

Compliance With the *Financial Information Act*, Regulation, and Directive

(Auditor General 1991 Annual Report, March 1991)

Recommendation of the Select Standing Committee on Public Accounts, June 1992 Report

Your Committee recommends that an amendment be made to the Financial Information Act *respecting the definition of "Corporation" as follows:*

> *"Corporation also means an organization or enterprise that is included in the reporting entity for purposes of the Government's summary financial statements."*

Response of the Ministry of Finance and Corporate Relations

The definition of "corporation" has not been amended in the Financial Information Act. *Some organizations which are included in the reporting entity for purposes of the government's financial statements are not suitable for reporting under the FIA due to the nature of their operations. The Office of the Comptroller General reviews the reporting entity on a regular basis to identify possible additions to the Act.*

Comment by the Office of the Auditor General on the Response of the Ministry

The recommendation has not been satisfactorily addressed, and the Ministry does not plan to take it forward for implementation. Reasons being given by the Ministry to support its position were previously discussed by the Committee before it decided to approve this recommendation.

Appendices

Appendix A

Compliance–with–Authorities Audits Completed 1990 to Date

1994/95: Report 5

Elevating Devices Safety Act

Travel Agents Act

Financial Administration Act: Guarantees and Indemnities

Land Tax Deferment Act

1993/94: Report 4

Statutory Tabling Requirements

Safeguarding Moveable Physical Assets

Treatment of Unclaimed Money

1993 Annual Report

Compliance with the *Financial Disclosure Act*

Order–in–Council Appointments

Compliance with Part 3 of the *Financial Administration Act*

Compliance with the *Tobacco Tax Act*

Financial Information Act: Follow–up

Small Acts

1992 Annual Report

Compliance with Part IV of the *Financial Administration Act* and its Related Regulations

1991 Annual Report

Compliance with the *Financial Information Act*, Regulation, and Directive

Compliance with Part IV of the *Financial Administration Act* and its Related Regulations

Appendix B

Office of the Auditor General: Audit Objectives and Methodology

Audit work performed by the Office of the Auditor General falls into three broad categories:

- Financial statement auditing;
- Value–for–money auditing; and
- Compliance–with–authorities auditing.

Each of these categories has certain objectives that are expected to be achieved, and each employs a particular methodology to reach those objectives. The following is a brief outline of the objectives and methodology applied by the Office for compliance–with–authorities auditing.

Authorities

Under our Canadian system of government, laws approved by parliament and provincial legislative assemblies are of paramount importance to our society.

Acts passed by the Legislative Assembly of British Columbia, including the Supply Acts, the *Financial Administration Act*, the *Financial Information Act*, and many others, provide the direction to the government and government organizations as to management of resources entrusted to them by the public, and the way in which they are to be held accountable to the Legislative Assembly for the execution of these responsibilities. These Acts provide the legal basis for funding, delivering and administering the Province's social, economic, environmental and other programs.

Accordingly, it is important that the government ensures compliance with these statutes and related authorities. It is also important that compliance with the statutes and related authorities be independently reviewed to ascertain whether public sector activities are carried out *intra vires*. This is where compliance–with–authorities auditing plays an important role.

Compliance–with–Authorities Auditing

Purpose of Compliance–with–Authorities Audits

The purpose of compliance–with–authorities audits is to provide an independent assessment as to whether or not legislative and related authorities are being complied with, in all significant respects.

However, we recognize that legislation and other related authorities may, over the course of time or due to other circumstances, become out of date or impractical in their application. Where we consider this to be the case, we will provide the appropriate additional commentary in our reports to draw attention to these difficulties.

In addition to separate compliance–with–authorities audits, the Office of the Auditor General also performs financial statement audits and value–for–money audits. While auditing for compliance with legislative and related authorities is the primary objective of compliance–with–authorities audits, auditing for compliance with authorities may also be included as part of financial statement audits or value–for–money audits where there are authorities that are relevant to the objectives of those audits.

Nature of Legislative and Related Authorities

Legislative and related authorities include legislation, regulations, orders in council or ministerial orders, directives, by–laws, policies, guidelines, rules and other instruments. Through these authorities, powers are established and delegated.

Legislation may delegate broad financial, operating and administrative powers to governments, ministers and officials who, in turn, may establish other related authorities, such as policies, to provide more detailed requirements that must be complied with by the organizations concerned. Such authorities are subordinate to enabling legislation and must not contradict or go outside the directions, conditions and limitations set out in that legislation.

This structure of authorities constitutes a basis for legislative control over the source, allocation and use of public resources, the operation and administration of programs, and the manner in which organizations are held accountable for the choices made in the exercise of their functions. The structure thus has pervasive effect on the activities of governments and other publicly accountable organizations. Authorities also form the basis for communication between elected officials and the bureaucracy.

Audit Standards

Auditors are expected to comply with established professional standards, referred to as generally accepted auditing standards. Our compliance–with–authorities audits are conducted in accordance with generally accepted auditing standards established by the Canadian Institute of Chartered Accountants (CICA). These consist of the general and examination standards in the CICA Handbook, and the reporting standards issued by the Public Sector Accounting and Auditing Board of the CICA.

Audit Selection

In general, we select specific sections in an act, or in several acts, having common objectives. In most instances, we do not audit all aspects of an act in the course of one audit.

The primary legislative instrument which provides for administration of the financial affairs of the Province is the *Financial Administration Act*. Therefore, compliance with this Act is of regular and ongoing significance to our Office. Other legislation and related authorities is considered for audit purposes on a more cyclical basis, depending

upon such factors as: the extent of impact on government, non–profit or private organizations and the public; the significance of financial accountability reporting requirements; the degree of interest by legislators and the public; and the likelihood and impact of non–compliance with legislated requirements.

Audit Process

The audit process adheres to the professional standards mentioned above. Of particular note is that compliance–with–authorities audits differ from other audits in their degree of dependence on the identification of relevant authorities and the interpretation of the meaning of the specific authorities being audited.

In order to identify the relevant authorities, the auditor must obtain an in–depth understanding as to how the authorities are themselves approved and how relevant authorities can be identified. The audit process includes determining that related authorities are within the limits prescribed by legislation, and that there are no obvious inconsistencies, contradictions or omissions in the authorities.

In addition, whether or not an authority is being complied with will often depend on its clarity, and the consistency in which its meaning is interpreted. Because of the importance of such interpretations, we seek professional legal advice where necessary.

In an examination designed to report on compliance with authorities, we seek reasonable assurance that the authorities have been complied with. Absolute assurance in auditing is not attainable because of such factors as the need for judgment, the use of testing, and the inherent limitations caused by differing interpretations in the meaning of authorities.

Reporting the Results of Audits

Our public report on each audit is in two parts: a formal audit report, showing the scope of the audit and our overall opinion on compliance, and a more detailed, explanatory report.

The formal report includes the auditor's professional opinion on whether or not the authorities that are the subject of the audit have been complied with, in all significant respects.

Our main considerations in assessing significance of non–compliance include monetary value, the nature of the authority or finding, and the context within which compliance is to occur.

In addition to the formal audit report, we provide a more detailed report that includes an explanation of what is required by the legislative and related authorities, the scope of our audit work, our overall observations, our detailed audit findings, and any other related observations.

When appropriate, we also make recommendations. The recommendations fall generally into three categories: to improve compliance with the legislative and related authorities; to improve operational effectiveness of the entity responsible for ensuring compliance; and, on occasion, to

provide useful, new legislative or related authorities.

There may be minor instances of non–compliance that either may not be detected by the audit or may not be worthy of inclusion in the report. We exercise professional judgement when assessing the significance of any non–compliance. For example, the needs of users of the report, the nature of the relevant authorities, and the extent of non–compliance must, among other things, be considered. As well, the significance of any non–compliance often cannot be measured in monetary terms alone.

We sometimes also issue a detailed management report of our findings to the ministry responsible for the legislation or the organizations affected by it. The relevant ministries or organizations are thus given an opportunity to respond to our findings, and we take this into account in the preparation of our public report.

When our public report on compliance–with–authorities audits completed in the past year is published, it is reviewed by the Select Standing Committee on Public Accounts of the Legislative Assembly of British Columbia. Recommendations made by the Committee in relation to our reports are followed up annually by our Office with the ministries responsible to obtain from them a status report on their progress in implementing the Committee's recommendations. These status reports are included in our next public report on compliance–with–authorities audits.

Appendix C

1994/95 Audit Reports Issued to Date

Report 1

Purchasing in School Districts

Report 2

Provincial Agricultural Land Commission

Report 3

Report on the 1993/94 Public Accounts,
Province of British Columbia

Report 4

Management of Government Debt

Report 5

Compliance–with–Authorities Audits

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