

## OCCASIONAL PAPER No. 10. B.C. GOVERNMENT FINANCES

### ACCOUNTING RULES OVER-STATE GOVERNMENT REVENUE ON ACTUAL CASH BASIS

Canadian public sector modified accrual accounting rules state that all of the net income (profit or loss) of self-supporting Crown corporations is to be included in the provincial consolidated revenue fund. However, as the actual cash transfer from BC Hydro and ICBC is usually significantly lower than the net income, the national accounting rules overstate the government's revenue on a cash basis.

In the case of BC Hydro, the payment to the government is limited to 85% of the net income, unless the resulting debt/equity ratio falls below 80/20. In recent years, despite high net income resulting from the liberal use of deferral accounts, the 85% dividend target has not been achieved because the debt/equity ratio would have been exceeded.

For ICBC, prior to FY2010/11 the government did not take any of the net income or capital reserve. In 2010 the government changed the Insurance Corporation Act to take all the Optional capital reserve beyond the capital management target set by the ICBC board (currently an MCT ratio of 260%). The Basic insurance net income and capital is excluded.

The equity (accumulated retained earnings and other components of equity) of BC Hydro and ICBC are counted as government assets. The provincial government has little investment in BC Hydro and none in ICBC.

Since FY2008/09 there has been a significant difference between the BC Hydro and ICBC net income recorded in the CRF compared to the actual cash transferred as a dividend or excess capital as summarized below (\$=millions):

Fiscal Year	Net Inc. HYDRO	Net Inc. ICBC	TOTAL	Actual Cash	DIFFERENCE
2016/17 Q1	684	(62)	622	259	363
2015/16	655	(293)	362	464	(102)
2014/15	581	659	1,240	403	837
2013/14	549	136	685	404	281
2012/13	509	231	740	215	525
2011/12	558	84	642	431	211
2010/11	599	323	922	1,039	117
2009/10	447	601	1,048	47	1,001
2008/09	365	512	877	nil	877

<b>TOTAL 09to16</b>	4,947	2,191	7,138	3,262	3,876
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Source: BC First Quarterly Report 2016/17, and Public Accounts 2015/16.

In this nine-year period the combined net income recorded was \$3.88 billion (or 119%) greater than the actual cash transferred.

## CHANGE IN ACCOUNTING RULES

The Budget Transparency and Accountability Act requires provincial self-supporting Crown corporations to use the accounting standards developed by the Canadian Institute of Chartered Accountants' public sector accounting board. Canada adopted the International Financial Reporting Standard (IFRS), which adds annual volatility due to the requirement to fully disclose liabilities. Until recently the IFRS rules did not recognize deferral accounts for regulated entities, such as BC Hydro. The provincial government allowed BC Hydro to retain its deferral accounts by adopting an American standard for these accounts (see Auditor General's 2011 report on BC Hydro's deferral accounts). In recent years, much of BC Hydro's net income and all of its dividend has been borrowed.

## DISTORTION OF GOVERNMENT REVENUE AND ASSETS

The provincial government has been recording the two Crowns' net income as revenue for over 10 years. From FY2008/09 to FY2016/17 (Q1 forecast) the accumulated net income of BC Hydro (bolstered by deferral accounts) will be approximately \$4.9 billion, while the actual payment to the government will be approximately \$2.6 billion. In the same period ICBC recorded some \$2.2 billion in net income while approximately \$1.2 billion will be transferred to the government. For the nine-year period the combined shortfall in actual cash transferred compared to the net income was approximately \$3.87 billion.

The planned phase-out of BC Hydro's dividend payment to the province beginning in 1018/19 will exacerbate the difference between the net income and the actual cash transfer.

In its first quarter 2016/17 financial forecast the government is forecasting a net surplus (after contingencies and forecast allowance) of \$541 million, assuming a combined net income from BC Hydro and ICBC of \$662 million. The forecast cash transfer is \$259 million after the government abandoned the planned \$150 million transfer of Optional insurance "excess" capital (the Optional capital has been re-assigned bolster the Basic capital). The \$403 million difference between the net income and the actual cash would

reduce the forecast government 2016/17 surplus to \$138 million if the government was recording the cash transfer, rather than the net income, from these two Crowns.

The current national accounting rules provide an incentive for the government to increase the net income from the self-supporting Crown corporations as this improves the government's surplus. If the government spent all of the net income recorded from BC Hydro and ICBC it would be forced to borrow the difference between the net income and the actual cash transfer.

In an email of May 6, 2015 to the writer Stuart Newton, the Comptroller General, stated that the government was not pursuing an amendment to the national accounting rules to address this distortion.

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The writer is a retired senior BC government public servant who's paper on the 40-year financial history of ICBC was published by *BC Studies* in 2013. The same academic journal will be publishing his paper describing the BC government's manipulation of the finances of BC Hydro from 2008 to 2014 in the fall. He has been an intervener in the BC Utilities Commission's 2014 and 2015 reviews of ICBC's rate requests.