

Standing Committee on Public Accounts

Third Report

December 2005

Auditor General's Report and Recommendations

1. The Standing Committee on Public Accounts of the Yukon Legislative Assembly accepts and endorses the recommendations made by the Office of the Auditor General of Canada in its reports on the Energy Solutions Centre Inc. and the Mayo-Dawson City Transmission Line Project.

2. The Committee is also encouraged by management's responses to these observations and recommendations. Based on the responses contained in the report, and the evidence provided by witnesses during the public hearings, the Committee is satisfied that the boards of directors and senior management responsible for the Yukon Development Corporation, the Yukon Energy Corporation and the Energy Solutions Centre Inc. have seriously considered the recommendations of the Auditor General. In many cases action to deal with the problems identified in the report has already been taken. In other cases action is being taken to comply with the Auditor General's recommendations.

3. The Committee is particularly pleased that the directors and senior management are putting effort into developing planning documents. This indicates a pro-active, rather than simply a reactive, stance one that will hopefully prevent problems from occurring in the future.

4. The Committee is also encouraged by management's response to the recommendations contained in the Public Accounts Committee's First Report and re-stated in paragraph 22 of the Auditor General's report.

5. The Committee also acknowledges the action taken by the Government of Yukon with regard to the Energy Solutions Centre Inc.

6. The Government of Yukon has announced that responsibility for the Energy Solutions Centre Inc. will be moved from the Yukon Development Corporation to the Department of Energy, Mines and Resources. This may indicate that the Government takes seriously the issues raised in the Auditor General's report and has seen the need to take action. However, as the details of the plan were not made clear to the Committee, the Committee cannot endorse this change.

Concerns

7. While endorsing the Auditor General's report the Committee also wishes to comment on certain concerns that emerged from the report and the public hearings.

Energy Solutions Centre Inc.

8. With regard to the Energy Solutions Centre Inc. the Committee's first and primary concern is the decision to create this entity "without informing the minister" responsible for it.¹ While there was no legal requirement to inform Cabinet the Committee considers it astonishing that the management and board of directors of the Yukon Development Corporation would consider it proper practice to create additional responsibilities for the minister responsible for the corporation without informing the minister of their intention to do so.

9. The Committee also notes that government corporations no longer have the ability to do this. As the Auditor General's report points out Section 3(1) of the *Corporate Governance Act* now "requires that new government corporations can only be established either through legislation or with the consent of the Commissioner in Executive Council."²

10. The Committee is also disturbed by the fact that establishing the Energy Solutions Centre Inc. as a separate subsidiary corporation enabled it to act according to a less restrictive legal environment than that which applies to the Yukon Development Corporation and the Yukon Energy Corporation (1-3 and 1-5).³

11. This less restrictive environment might have, in theory, facilitated the centre's work by providing it with greater freedom of action. However, this lack of restriction instead manifested itself in inadequate management and inadequate reporting to the board of directors. (1-1)

12. A third concern is that of board capacity: the ability of members of the boards of directors of government corporations to carry out their duties. Evidence presented to the Committee at the public hearing suggested that members of the Energy Solutions Centre Inc. board of directors lacked the qualifications needed to oversee this kind of enterprise. In response the Corporation has now committed itself to more extensive, and on-going, training for board members. (1-6, 1-7)

13. Further, it appears that directors were not clear as to their responsibilities with regard to this entity. As a result directors did not ask for information they should have asked for and did not "challenge management action" when they should have. (1-1)

14. Another concern is that "Management did not inform the company's board of directors of many of its significant actions." (1-1) While directors have a duty to ask the right questions management also has a duty to disclose relevant information to board members, even if that information is not explicitly requested.

¹ Office of the Auditor General of Canada, *Energy Solutions Centre, Inc.* February 2005, page 6.

² Office of the Auditor General of Canada, *Energy Solutions Centre, Inc.* February 2005, page 7.

³ Numbers in brackets indicate page references in the transcript of public hearings held February 8 and 9, 2005 and appended to this report.

15. A final concern is an apparent lack of formal records surrounding decisions that were taken and what information was reported to whom. For example, David Morrison, President and Chief Executive Officer of the Yukon Development Corporation, informed the Committee that “either late November, early December in the year 2000, the (Yukon Development Corporation Board of Directors)...approved the establishment of the (Energy Solutions Centre Inc.). I can’t tell you what was explained to the board. The minutes don’t reflect that kind of detail.” (1-12)

16. Responses provided to the Committee in the public hearings also indicated a lack of formal communications and reporting from management to the board of directors and from there to the minister responsible for the corporation. For example, Mr. Morrison said he could find no evidence that the minister responsible for the Yukon Development Corporation was ever asked for approval in establishing the Energy Solutions Centre Inc. (1-12)

17. Willard Phelps, Chair of the Yukon Development Corporation Board of Directors, informed the Committee that as Chair, he “would want to see that type of direction contained in a letter of expectation from the minister.”(1-3) The Committee notes that the Government of Yukon and the Yukon Development Corporation have now concluded protocols that outline roles, responsibilities and expectations. These protocols are appended to the Committee’s Second Report.⁴

Mayo-Dawson City Transmission System Project

18. The Committee’s primary concern with this project was that “Yukon Energy Corporation’s board of directors was not fully briefed by management about the risks of using the chosen construction method, something called design/build.” (2-1)

19. What is most disturbing is that it appears management deliberately did not inform the board that the engineering firm hired to do preliminary engineering and cost estimates – BC Hydro International – “cited many disadvantages and few advantages to using the design-build method for this project.”⁵ Instead board members were, according to Mr. Morrison’s understanding, presented only with management’s preferred option – design/build. That, in turn, became the board’s recommendation to the minister responsible for the corporation. (2-4)

20. As stated in paragraph 14 above board members have a duty to be thorough and ask the right questions of management. However, management also has a duty to disclose relevant information to board members, even if that information is not explicitly requested.

21. This apparently deliberate lack of disclosure leads to a serious problem that touches on fundamental aspects of the relationship between government and

⁴ Standing Committee on Public Accounts of the 31st Yukon Legislature, Second Report, April 2005, Appendix A and Appendix B.

⁵ Office of the Auditor General of Canada, *Mayo-Dawson City Transmission System Project*, February 2005, page 7.

government corporations. Because the board of directors does not appear to have been fully informed of BC Hydro International's assessment the chair of the board could not pass that information on to the minister responsible for the corporation. The minister had the responsibility for approving the project, but given the evidence presented to the Committee, it seems that approval was not fully informed.

22. One of the fundamental principles of parliamentary government in Yukon is that of ministerial responsibility: that a minister of the government is ultimately responsible for the performance of government departments and corporations, even though those entities are run on a daily basis by professional civil servants.

23. This principle is somewhat different when it comes to government corporations that are designed, unlike departments, to operate at arm's length from government. As in the case of the Yukon Development Corporation and the Yukon Energy Corporation a board of directors acts as an intermediary between senior managers and the minister.

24. While there are sound reasons for having an arm's length relationship between Cabinet and government corporations, this distance should not be the result of keeping the board, and ultimately the minister, uninformed about those aspects of corporate activities they should be informed about. If that is the case ministerial responsibility becomes attenuated and a fundamental principle of government risks being lost.

25. As Members of the Legislative Assembly, Committee members take this issue most seriously. The Assembly cannot perform its role as a forum for government accountability if government ministers are not properly informed.

26. The Mayo-Dawson City Transmission System Project also suffered from inadequate reporting with regard to financial and management issues. Progress reports presented to the board of directors tended to take a "narrative" form, rather than a thorough reporting of financial information. (2-11) Also, important decisions and significant problems were not reported to the board.

27. In attempting to explain the Auditor General's conclusion that the project was poorly managed, Mr. Morrison said, "there seemed to be an urgency...at the management level." (2-12) It is surmised that the desire to get the project done led to improper management practices, such as the over-use of sole-source contracts and contracting with contractors who had no demonstrated experience in transmission line construction. (2-13)

28. In this regard the Committee would state that while completing projects quickly can be a desirable goal this should not be done at the expense of proper managerial and reporting practices. Corporate managers and boards of directors must consider the following of proper procedure and the ensuring of accountability as valuable aspects of project management.

29. This project was also hampered by the high degree of turnover amongst those most responsible for it. From the inception of the project in August 2000 to its completion in January 2004 the project was overseen by four ministers, three board chairs and a similar number of corporate presidents.

30. Circumstances may result in a high turnover of key personnel that cannot be prevented. However, the potential for such turnover reinforces the need for full records of decision-making to be kept and that all elements in the decision-making chain – senior management, the board of directors, the minister's office – be kept fully apprised of decisions being taken and the status of projects.

31. The Committee would also note that the Auditor General's report on this project raised concerns for the Committee regarding board capacity. Mr. Morrison confirmed for the Committee that none of the Yukon Energy Corporation Board members had expertise in electrical engineering or project management. While he and Mr. Phelps agreed having such expertise would have been an asset for the board, they did not believe this was an insurmountable problem. The key, according to Mr. Morrison is for the board to address its "skills gap" by, for example, contracting independent, expert advice. In fact, the Yukon Energy Corporation Board "retained the services of a technical advisor" in relation to this project. In that sense Mr. Morrison and Mr. Phelps did not see board capacity as the crucial issue. According to Mr. Phelps the problem was "whether (board members) were actively discharging their responsibilities and clearly understood them." (2-5, 2-6) The Auditor General's report leads the Committee to the conclusion that there was some deficiency in this regard.

Conclusions and Recommendations

32. In its First Report the Standing Committee on Public Accounts made nine recommendations.

33. As will be seen most of these recommendations have to do with the governance of government corporations. Considering the content of the two reports of the Auditor General, the Committee re-emphasizes these recommendations.

34. During the Public Accounts Committee hearings held in February 2004 the issue of board governance may have appeared a rather abstract issue. The reports before the Committee in February 2005 illustrate that these concerns can no longer be viewed as abstractions.

35. The events detailed in the reports of the Auditor General show clearly that the failure of board governance was a contributing factor to the problems that occurred. The reports focus on issues related to the boards of directors of the Yukon Development Corporation, the Yukon Energy Corporation and the Energy Solutions Centre Inc. However, the Committee believes these reports and their recommendations, and this report and its recommendations, should be taken seriously by all entities that operate at arm's length from government.

36. The first recommendation of the First Report was “That the Cabinet, in consultation with the boards of directors and the general public, review the criteria for appointment to these boards of directors.”

37. Before discussing this recommendation in detail the Committee would like to state clearly that it values the contribution that Yukoners make when they agree to take on the position of director of those entities associated with the Government of Yukon. This level of governance is essential to the proper functioning of these entities. While problems must be acknowledged, the observations and recommendations in this report are made in the hope that they will help directors in performing their duties.

38. The issue of the expertise and experience of individuals appointed to boards of directors was much discussed during the public hearings. While having directors with appropriate expertise and experience was acknowledged as an asset it was also pointed out that the Government of Yukon has a small pool of individuals to draw from in making appointments.

39. For this reason the Committee believes that individuals with appropriate expertise and experience should be sought for appointment. However, given the inability of all boards to be filled with individuals who will have the broad range of expertise and experience needed to fully encompass the mandates of these boards, the Committee believes that other things must be emphasized.

40. First, individuals solicited to sit on boards of directors must be fully apprised, before they accept an appointment, of the expectations that will be placed upon them as directors.

41. Second, board members must receive appropriate and on-going training in order to deal with issues before them.

42. Third, boards of directors should employ expert advisors where necessary. Such expertise should be provided by individuals not associated with the entity the board oversees. Appropriate administrative and financial resources should be made available to boards of directors so they can carry out their oversight duties.

43. Employing independent advisors should not be taken as an indication of distrust between a board of directors and senior management. Since the employment of advisors will be the exception, not the rule, there must be a high degree of trust between boards of directors and senior management. However, directors must be prepared to employ informed, constructive scepticism in defence of the public interest.

44. The second recommendation of the First Report was “That the Cabinet review the method of appointment of the chairs of the governing boards and the operational heads of these entities.”

45. The Committee did not address the issue of the method of appointment of the chairs of boards of directors and the operational heads of government related entities during these hearings. Nonetheless the Committee would reiterate this recommendation as it fits with other recommendations regarding the governance of government related entities.

46. The third recommendation of the First Report was “That the Legislative Assembly consider establishing a Standing Committee on Appointments to Major Government Boards and Committees.”

47. It should be noted that during the public hearings the Chair of the Board of Directors of the Yukon Development Corporation said that in his view the time had come to end partisanship in board appointments. (2-23) This opinion is significant given that the board chair is a former Premier and former minister responsible for the Yukon Development Corporation.

48. The Committee views the establishment of the above-mentioned standing committee as the proper mechanism for removing partisanship from the appointment process.

49. The fourth recommendation of the First Report was “That the entities examined in this report confer on best practices for the training of board members; and that training regarding the potential financial liability of board members be a part of that process.”

50. The Committee is satisfied that the Yukon Development Corporation and its subsidiaries are taking the issue of board training seriously. The Committee was also pleased to learn that this training is being co-ordinated with the Yukon Housing Corporation.

51. It was not clear from the evidence presented that this training would address financial liability for board members. If that issue is not currently part of the training program the Committee would, again, recommend that it become so.

52. The fifth recommendation of the First Report was “That the planning and accountability documents employed by the entities examined in this report contain performance measures and expectations and that the plans be tabled in the Legislative Assembly annually.”

53. The Committee is satisfied that those responsible for the Yukon Development Corporation and its subsidiaries are seriously addressing the issue of planning, accountability and performance measurement. The Committee is hopeful that these will be reported to the Legislative Assembly on a regular basis.

54. The sixth recommendation of the First Report was “That the Cabinet review the *Financial Administration Act* and consider amending it to incorporate requirements

similar to those applicable to Crown corporations found in the federal *Financial Administration Act*.”

55. Part X of the federal *Financial Administration Act* addresses several issues that are germane to corporate governance. The Committee would reiterate its recommendation that the Yukon Cabinet examine this legislation and incorporate into Yukon law those elements that would enhance corporate functioning and accountability. This incorporation could take the form of amendments to the Yukon’s *Financial Administration Act* or the *Corporate Governance Act*.

56. In its review of corporate governance the Government of Yukon should also consider other developments at the federal level. On February 15, 2005 the Office of the Auditor General of Canada released a status report, following up on issues raised in previous reports. Chapter 7 of this report deals with the Governance of Crown Corporations. Several of the issues dealt with in this chapter are relevant to the issues raised during this Committee’s public hearings.

57. On February 17, 2005 federal Treasury Board President Reg Alcock released “Review of the Governance Framework for Canada’s Crown Corporations – Meeting the Expectations of Canadians.” This document also addresses issues raised in our public hearings.

58. While the Committee is reluctant to recommend specific measures based on these documents, we would suggest strongly that these documents be consulted in any review of corporate governance in Yukon.

59. The seventh recommendation of the First Report was “That the Cabinet, the Yukon Legislative Assembly and the heads of the entities examined in this report establish a process to evaluate mandates and consult with the Yukon public in doing so.”

60. The reports of the Auditor General and the public hearings did not directly address corporate mandates. However, one of the issues raised in the hearing on the Energy Solutions Centre Inc. was that entity’s mandate and whether all the projects it undertook fell within its mandate. This led to other issues being raised, such as the manner and the extent to which the centre’s mandate was articulated and how involved the board of directors and the minister responsible were in authorizing the expanding mandate.

61. Once again, this case strongly suggests that assessing the mandates of government related entities is not an entirely abstract issue. As a result the Committee would also re-iterate this recommendation.

62. The eighth recommendation of the First Report was “That the ministers responsible for the Yukon Housing Corporation, the Yukon Liquor Corporation and the

Yukon Development Corporation ensure that protocols are negotiated annually, as per Section 4(2) of the *Corporate Governance Act*.”

63. At its hearing with the president and chief executive officer of the Yukon Development Corporation on November 19, 2004 the Committee learned that such a protocol had been negotiated.

64. The Committee is encouraged that the Chair of the Board of Directors and the president and chief executive officer are strongly supportive of the protocols. (1-9, 1-13, 2-27)

65. The Committee is less encouraged by the fact that the protocol has yet to be tabled in the Legislative Assembly, though the Shareholders Letter of Expectations between the Minister responsible for the Yukon Development Corporation and the corporation and its subsidiaries was tabled during the 2004 Fall Sitting.

66. Given the importance of this document the Committee makes the following recommendation:

Recommendation #1: That the protocol negotiated pursuant to Section 4(2) of the *Corporate Governance Act* be tabled in the Legislative Assembly at its next Sitting.

67. The Committee also notes that Section 4 of the *Corporate Governance Act* gives the Commissioner in Executive Council the authority to “issue directives to a government corporation with respect to the exercise of the powers and functions of the corporation.” Subject to such a directive the minister responsible for the corporation and the corporation “shall negotiate annually a protocol about performance expectations for the corporation to meet and the roles of the Minister, board, and president respectively, in the work of the corporation...” This section further requires that “a directive under this section...shall be tabled in the Legislative Assembly forthwith after being issued.”

68. While this section requires the tabling of the minister’s directive it does not require the tabling of the protocol itself. Therefore the Committee further recommends:

Recommendation #2: That all subsequent protocols for the Yukon Housing Corporation, the Yukon Liquor Corporation and the Yukon Development Corporation be tabled in the Legislative Assembly as soon as practicable;

Recommendation #3: That the Government of Yukon undertake to amend the *Corporate Governance Act* to require the tabling of such protocols in the Legislative Assembly; and

Recommendation #4: That the Government of Yukon ensure that all directives issued pursuant to Section 4 of the *Corporate Governance Act* are tabled in the Legislative Assembly as required by the Act.

69. The ninth recommendation of the First Report was “That the Legislative Assembly find an acceptable method to ensure a higher level of accountability for the entities examined in this report takes place on a more regular basis.”

70. The Standing Committee on Public Accounts of the 31st Yukon Legislature has devoted its public hearings in 2004 and 2005 to dealing with government related entities. This is valuable work that the Committee readily undertakes. However, the mandate of the Committee goes beyond that of government related entities.

71. The chair of the Yukon Development Corporation Board of Directors and the corporation’s president and chief executive officer appeared in the Legislative Assembly in Committee of the Whole in 2004 and 2005. This is an example of the kind of action the Legislative Assembly can take to assist the Committee in ensuring a high level of accountability for government related entities.

72. In closing, the Committee would again draw attention to the support offered by the Office of the Auditor General of Canada for the recommendations contained in the First Report of the Standing Committee on Public Accounts. In its report on the Energy Solutions Centre Inc. the Auditor General said, “These recommendations indicate areas where governance of entities such as the Energy Solutions Centre Inc. and the Yukon Development Corporation can be improved. The Legislative Assembly, the Government of Yukon, and government corporations should seriously consider these recommendations.” As part of one of its recommendations the Auditor General said the Government of Yukon should follow the recommendations in the Committees first report and “examine the legislative framework, governance structure, and accountability relationships for its government corporations and their subsidiaries.”⁶

⁶ Office of the Auditor General of Canada, *Energy Solutions Centre, Inc.* February 2005, pages 5-6.