

Chapter 2

Financial Assistance to Atcon: Unanswered Questions

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Financial Assistance to Atcon: Unanswered Questions

Unanswered Questions

2.1 In our 2015 report *Financial Assistance to Atcon Holdings Inc. and Industry*, we reported on significant financial assistance granted to the Atcon group of companies by the Province. Just nine months after receiving a \$50 million guarantee from the Province, Atcon was placed in receivership.

2.2 Following Atcon's bankruptcy in 2010, the Province was left with close to \$70 million in unrecovered funds. The focus of our 2015 report was the events surrounding government's decision making process in granting financial assistance to Atcon¹ in 2008 and 2009, as well as how to improve the performance of the Department of Economic Development.

2.3 We reported:

- most internal processes at the (then) Department of Economic Development worked as designed, though we did identify a number of areas for improvement;
- Cabinet approved financial assistance to Atcon despite significant risk to taxpayers and numerous, repeated warnings by civil servants;
- Cabinet later removed a number of terms and conditions that were put in place to mitigate the Province's risk, the most significant of which was to release its first security interest position in favour of the Bank of Nova Scotia; and
- These findings showed Cabinet displayed a very

¹ Unless otherwise indicated, when we use Atcon in this report we are referring to Atcon Holdings Inc.

troubling disregard for taxpayers' money.

2.4 At the time of the release of the 2015 report, we were also left with many unanswered questions, such as where did the money go? This is the most common question we receive from concerned citizens on the Atcon file. Our office has received numerous phone calls, emails and letters regarding this file. The questions on the use of the funds received by Atcon, and whether anyone benefited inappropriately from this money, are key concerns given the short timeframe between granting the company financial assistance and the placement of Atcon into receivership. This report will respond, to the best of our ability, to these unanswered questions.

Examination Objectives

2.5 The objectives of our special examination were:

- To determine how the \$63.4 million in financial assistance provided to Atcon was spent; and
- To determine if anyone benefited inappropriately from the \$63.4 million in financial assistance.

Assessment criteria

2.6 In assessing the objectives of our examination, we considered the following criteria:

- Atcon payments should be supported by proper documentation such as invoices, legal agreements, or other records;
- Atcon payments should be made to a legitimate vendor;
- Atcon payments should be recorded in Atcon's financial statements; and
- Payments made to the Government of Northwest Territories should be supported by documents and analysis.

Conclusions

2.7 We concluded, based on the information we were able to obtain, \$63.4 million in funds provided to Atcon appear to have been largely used for business related activities. However, there was a significant amount of information that we were unable to examine, including bank statements and cancelled cheques for key Atcon companies such as Atcon Holdings and Atcon Industrial (as described in paragraph 2.34). Our testing of cheques cashed between July 2009 and March 2010 did not reveal any large or unusual payments to owners of Atcon, or companies it is known to control, as a result of receiving \$63.4 million in assistance.

**Summary of
Results in
Brief**

2.8 A summary of our results in brief is presented in Exhibit 2.1.

Exhibit 2.1 - Summary of results in brief

Financial Assistance to Atcon: Unanswered Questions

Why Is This Important?

- Following Atcon's bankruptcy in 2010, the Province was left with close to \$70 million in unrecovered funds.
- After our initial 2015 Atcon report, many unanswered questions remained such as: where did the money go? Did anyone benefit inappropriately?
- The public remained concerned, as our office continued to receive numerous phone calls, emails and letters regarding this file.

What We Found

Overall Conclusions

- We concluded, based on the information we were able to obtain, \$63.4 million in funds provided to Atcon appear to have been largely used for business related activities.
- However, we found questionable Atcon operating and financial reporting practices.
- We cannot conclude all NB suppliers were paid as per Atcon's declaration.
- Only 4 of 19 recommendations from our 2015 report have been implemented by Opportunities NB (ONB).

Where did the \$63.4 million go?

A breakdown on how the money was used (in millions):

- \$21.4 to pay off high interest loans
- \$14.6 to pay down operating line of credit
- \$13.4 paid to the Government of Northwest Territories for the Deh Cho Bridge guarantee (*ONB obtained support for payment some six years after*)
- \$9.8 to fund ongoing operations of Atcon
- \$2.9 to pay other fees and taxes
- \$1.2 to pay liens and judgments from creditors

Did Anyone Benefit Inappropriately?

During the period of 2008-2010 when Atcon was seeking financial assistance:

- \$735,000 of personal expenses (travel, RRSP, luxury car, properties, jewelry, etc.) were paid through Atcon accounts
- Some family members of some key senior management were salaried, with little evidence they did any work for Atcon
- Atcon had a corporate jet with an operating cost of over \$8 million

\$50 Million of New Debt Wasn't the Solution

- Atcon had growing debt, insufficient working capital, severe cash shortage and assistance mostly paid off existing debt.
- Irregularities in audited financial statements improved Atcon's financial position in appearance.

Limited Progress on 2015 AGNB Recommendations

- ONB has been making progress in the development of policies and guidelines
- ONB reported it implemented 15 of our 19 recommendations, however we determined that number is 4 of 19 or 21%
- We found little effort by Executive Council Office to ensure our recommendations have been applied to all other entities providing financial assistance to industry even though over \$300 million has been given since the 2015 report.

Release of Security Held by Province

- Cabinet Ministers we interviewed offered no clear rationale for their decision.
- Had the security not been given up, we believe the Province could have recovered in the range of an additional \$12-19 million.

Results in Brief

Where did the \$50 million go?

2.9 Based on our review, a significant amount of the \$50 million received by Atcon (\$14.6 million) was used to pay down the company's operating line of credit, bringing Atcon back within the limits of its borrowing base calculation². The remaining amount was used to pay off high interest loans from other lenders (\$21.4 million), liens and judgments from creditors (\$1.2 million) and other fees and taxes (\$2.9 million). The remainder, close to \$10 million, appeared to be used to fund ongoing operations of Atcon.

Where did the \$13.4 million go?

2.10 A total of \$13.4 million was paid to the Government of Northwest Territories (GNWT) in 2010 in connection with the \$13.4 million guarantee on the Deh Cho Bridge to cover deficiencies in the construction of the bridge by Atcon. The GNWT provided Opportunities NB (ONB) with an accounting of the costs, including support, in 2016. At the time of our examination, ONB had not completed its review of the supporting documents; therefore, we are unable to confirm that payment to GNWT was supported.

Which suppliers were paid

2.11 For the companies examined at the year ended January 31, 2009, a total of 1,446 suppliers were listed in Atcon's payment register for \$148 million; 33% (\$49 million) of this amount was for New Brunswick³ suppliers. For the year ended January 31, 2010 there were 1,026 suppliers listed on the payment register for just over \$33 million; 37% (\$12 million) of this amount was for NB suppliers.

We cannot conclude all NB suppliers were paid as per condition of financial assistance

2.12 One of the conditions of the guarantee agreements was for Atcon to pay all outstanding payables owed to a specified number of New Brunswick companies, a total of \$6.5 million. The company provided a statutory declaration to the Province asserting that Atcon had "authorized and caused to be paid those payments".

2.13 We attempted to verify these amounts were indeed paid as indicated. Following our analysis, we were able to conclude 67 of 314 (21%) New Brunswick suppliers received the amount they were owed (\$1.2 million), but we are unable to

² A borrowing base is the amount of money a company can borrow based on the value of its collateral.

³ The province of origin was determined based on the telephone number (area code) in the vendor master file in Atcon's records.

conclude whether all remaining NB suppliers received payment as there was insufficient information to trace all payments.

***Personal expenses
paid through
company accounts***

2.14 Our review of credit card activity and activity in the shareholder account indicates certain individuals put personal expenses through company accounts. We estimate this amount to be \$735,000 for the years ended January 31, 2008 to January 31, 2010, when Atcon was seeking or received significant financial assistance from the Province. These consisted of luxury car lease payments, RRSP contributions, purchase of properties in NB, personal income tax payments, vacation property in Aruba and jewelry.

2.15 We also examined the use of Atcon's corporate jet, acquired in 2007 with a seating capacity of 20. The jet was used for flights to areas such as Fort McMurray, Calgary and Toronto, and typically carried Atcon executives and/or construction staff. The direct cost of operating the jet was over \$8 million for the period of January 31, 2008 to January 31, 2010. Records indicate the jet was used on occasion for personal reasons, but we were unable to quantify the personal benefit received because we didn't have sufficient information to do so.

2.16 We noted compensation to three key executives ranged, in total for the group, between \$554,000 and \$603,000 annually between 2007 and 2009. We also found there were annual increases during this period of 4% to 5%. This increase was not significant enough, in our opinion, to indicate an inappropriate benefit. We also found that some family members of some of the key executives received salaries from Atcon, though we found little evidence that certain family members had a regular or sustained presence at Atcon. Total annual compensation to this group of family members ranged between approximately \$340,000 and \$378,000 between 2007 and 2009. We considered some of the compensation paid to family members as significant given what appeared to be limited involvement with the company.

***\$50 million in new
debt was not the
solution***

2.17 Based on our work, we believe Atcon's financial problems were due largely to a history of poor working capital management and insufficient capital to support the rapid increase in business volume beginning in 2007.

2.18 Our analysis indicates the additional \$50 million in debt taken on by Atcon in July 2009 was not sufficient to save the

company from its eventual failure. Atcon was experiencing significant cash flow issues and was in violation of its debt covenants when it received the \$50 million from the Bank of Nova Scotia (guaranteed by the Province). Rather than a \$50 million cash injection for operations, the majority of the \$50 million in financing was used to pay down a line of credit and existing high interest debt, as well as various fees, taxes, liens and judgments. A Memorandum to Executive Council dated August 31, 2009 describes Atcon's financial situation: "as of August 2009, Atcon is cash strapped and \$20+ million over its borrowing base with the bank."

Review of internal correspondence identifies poor practices

2.19 Atcon was operating under significant cash flow stress in 2009. A review of internal correspondence identified the following issues:

- poor project management practices which lead to higher project costs;
- poor cost control on jobs;
- bounced cheques to suppliers, and contractors and suppliers who are unable to collect on their accounts; and
- cheques not issued due to lack of cash.

Financial analysis identifies serious concerns

2.20 Our analysis of the consolidated financial statements from January 31, 2004 to January 31, 2009 shows a company with a growing amount of debt, insufficient working capital and a severe cash shortage:

- In 2009, Atcon's debt was 3 times larger than its equity, and the company's debt-to-equity ratio was double the industry average.
- Atcon was increasingly using debt to fund day-to-day operations. The company was consistently and increasingly in a negative cash position from 2004 to 2009.
- Revenues increased significantly between 2004 and 2009, but the profit margin was decreasing, from 22% in 2004 to 9% in 2009.
- As Atcon's debt continued to grow, interest and bank charges began outpacing earnings from operations in 2008 and 2009.

***Irregularities noted
in January 31, 2009
financial statements***

- 2.21** During our analysis, we noted two significant but related irregularities in the audited financial statements of Atcon Holdings at January 31, 2009:
- Discrepancy of \$23 million between the balance sheet and the statement of cash flow; and
 - Questionable reclassification of \$21.7 million (of short term accounts payable to long term liabilities).
- 2.22** As a result of the discrepancy between the balance sheet and cash flow statement, the cash flow statement shows positive cash flows from operations (while previous years statements show negative cash flows from operations). Had the reclassification been carried over to the cash flow statement, it would have instead showed negative cash flow from operations.
- 2.23** The questionable reclassification improved the financial position (in appearance) of the company by improving its current ratio⁴, a key measure used to assess the liquidity and credit worthiness of a company, as well as its ability to pay its bills. It should be noted that Grant Thornton, Atcon's auditors, provided an unqualified (clean) opinion on Atcon's financial statements.

***Cabinet members
knew risks of
assisting Atcon***

- 2.24** We met individually with each of six Cabinet Ministers who were part of the decision to provide \$50 million in loan guarantees to Atcon in July 2009, and the subsequent decision to release the Province's security in favour of the Bank of Nova Scotia.
- 2.25** The Ministers described the current process for reviewing requests for assistance as more robust, and they affirmed they understood the risks involved with the request from Atcon and spent significant time discussing the file.
- 2.26** It appears the decision was due to a number of factors including a depressed economy in Miramichi and the large number of businesses that would be negatively affected by Atcon's failure. While the Cabinet Ministers provided a

⁴ Current ratio (total current assets divided by total current liabilities) measures the ability of an organization to pay its bills in the near-term. Source: www.accountingtools.com/current-ratio

consistent rationale for providing the assistance, no clear rationale was provided for the decision to release security in favour of the bank.

Province has only recovered 4.5% while Bank has recovered close to 80%

2.27 Through the receivership process, Atcon’s bank has recovered close to 80% (\$77.2 million) of the amount owed from Atcon while the Province has recovered an estimated 4.5% (\$2.8 million). Had Cabinet not given up the Province’s security in favour of the Bank of Nova Scotia, we believe the Province could have recovered in the range of an additional \$12-19 million.

Follow up of 2015 recommendations

2.28 We reviewed the updates provided by Opportunities NB (ONB) on the status of the recommendations made in our 2015 audit *Financial Assistance to Atcon Holdings Inc. and to Industry*. We examined the new or improved initiatives discussed by ONB and tested a sample of assistance files to assess their implementation.

Although ONB has made progress, only 4 of 19 recommendations from our 2015 Atcon report have been implemented

2.29 Of the 19 recommendations made in our 2015 report, ONB reported 15 as implemented and four as “in-progress.” However, following our review, we determined ONB has implemented only four of our recommendations, as shown in Exhibit 2.2. For the remaining 11 recommendations, we found ONB made progress in the development of policies and guidelines, but during testing we found exceptions in the application of the new policies, resulting in a finding of “not implemented.”

Exhibit 2.2 - Summary of implementation status of recommendations from 2015 report on Financial Assistance to Atcon Holdings Inc. and to Industry

Summary of implementation status of recommendations from 2015 report on Financial Assistance to Atcon Holdings Inc. and to Industry		
	As assessed by ONB	As assessed by AGNB
Recommendations implemented	15	4
Recommendations not implemented	4	15
Total recommendations	19	19

Chart created by AGNB

Recommendations 2.30 A summary of our recommendations can be found in Exhibit 2.3.

Exhibit 2.3 - Summary of Recommendations for scenarios where financial assistance requested is of a significant amount and is considered high risk

Recommendation	Department's response	Target date for implementation
<p>2.80 We recommend, for performance bonds or funds placed in trust, Opportunities NB structure the release of such funds such that sufficient supporting documentation is obtained and reviewed for authenticity and legitimacy prior to authorizing the disbursement of funds.</p>	<p><i>ONB agrees with this recommendation and will implement for all future performance bond and in-trust arrangements.</i></p>	<p><i>Already being done where required</i></p>
<p>2.150 Where the financial assistance requested is significant and is considered high risk, we recommend a clear determination be made and presented to Cabinet as to whether the financial assistance requested is sufficient for the purpose intended.</p>	<p><i>ONB agrees with this recommendation and does consider the adequacy of the funding requested when making its assistance decisions.</i></p>	<p><i>Already being done where required</i></p>
<p>2.152 Where the financial assistance requested is significant and is considered high risk, we recommend information presented to Cabinet for decisions on financial assistance should include comparisons to industry standards to assess the health of the company requesting financial assistance.</p>	<p><i>ONB agrees with this recommendation. Since readily available market based comparables are usually geared towards larger companies on a national or international basis, ONB will look to implement this recommendation on larger credits where warranted.</i></p>	<p><i>Already being done where required</i></p>
<p>2.154 Where the financial assistance requested is significant and is considered high risk, we recommend no financial assistance be granted to a company when significant amounts are outstanding from the shareholders of the company or from affiliated companies. Any exceptions should be rare and well justified.</p>	<p><i>ONB agrees with this recommendation and currently does not allow funding to companies with unwarranted (non-business reasons) balances due to/from any related party. Only in a rare and well justified circumstance would this be permitted.</i></p>	<p><i>Already being done where required</i></p>

Exhibit 2.3 - Summary of Recommendations for scenarios where financial assistance requested is of a significant amount and is considered high risk (continued)

Recommendation	Department's response	Target date for implementation
<p>2.156 Where the financial assistance requested is significant and is considered high risk, we recommend management and shareholders be required to make a declaration pertaining to dividends, salaries, bonuses (or other) as needed, as part of the application process, such as:</p> <ul style="list-style-type: none"> • Salaries to key executives for the past three to five years; • Salaries, dividends and bonuses to shareholders and family members for the past three to five years; • Transfers to related/associated/affiliated companies in the past three to five years; • Details of shareholder account activity during the past three to five years; and • Details of dividends, share redemptions and changes in share capital in the past three to five years. 	<p><i>ONB agrees with this recommendation and currently reviews payment history to related parties/entities.</i></p> <p><i>ONB's current practice in credit agreements is to require:</i></p> <ul style="list-style-type: none"> • <i>Balances to be postponed and subordinated;</i> • <i>Outstanding amounts to be repaid;</i> • <i>Restrict payments to related parties;</i> • <i>Limit future pay increases; and,</i> • <i>Limit sale/encumbrance of assets.</i> 	<p><i>Already being done where required</i></p>
<p>2.158 Where the financial assistance requested is significant and is considered high risk, we recommend that agreements contain a restriction to require the approval of ONB prior to a dividend or bonus payment.</p>	<p><i>ONB agrees with this recommendation and currently reviews payment history to related parties/entities.</i></p> <p><i>ONB's current practice in credit agreements is to require:</i></p> <ul style="list-style-type: none"> • <i>Balances to be postponed and subordinated;</i> • <i>Outstanding amounts to be repaid;</i> • <i>Restrict payments to related parties;</i> • <i>Limit future pay increases; and,</i> • <i>Limit sale/encumbrance of assets.</i> 	<p><i>Already being done where required</i></p>

Exhibit 2.3 - Summary of Recommendations for scenarios where financial assistance requested is of a significant amount and is considered high risk (continued)

Recommendation	Department’s response	Target date for implementation
<p>2.160 Where the financial assistance requested is significant and is considered high risk, we recommend that statutory declarations made as a condition of financial assistance be verified.</p>	<p><i>ONB agrees with this recommendation and currently requires at least an annual review of all declarations/covenants/requirements in agreements.</i></p>	<p><i>Already being done where required</i></p>
<p>2.162 Where the Province has personal guarantees as security on financial assistance, we recommend ONB put in place a process whereby, in the event of default by the recipient, personal guarantees are promptly pursued.</p>	<p><i>ONB agrees with this recommendation and will institute a process with our legal counsel to pursue any and all security as soon as legally prudent and in the best interests of the Province.</i></p>	<p><i>Already being done where required</i></p>
<p>2.164 We recommend the Executive Council Office take responsibility for coordinating the implementation of recommendations in this report by all departments/agencies providing financial assistance to industry.</p>	<p><i>The Executive Council Office agrees with this recommendation. It will work with ONB to adapt, for use by other departments and agencies that provide financial assistance, the policies and processes established by ONB to address the recommendations.</i></p>	<p><i>The policies and processes will be adapted and rolled out to other departments and agencies within six months of being established and tested by ONB.</i></p>

Scope

2.31 Our work included:

- Examination of electronic files on hard drives obtained from Atcon computers held by the receiver. We made copies of the hard drives, and examined over 15,000 files.
- Analysis of data included in the financial software of Atcon (accounting books and records), copied from an Atcon server held by the receiver.
- In-depth analysis of Atcon's audited financial statements for the years ended January 31, 2004 to January 31, 2009.
- Indexing and search of over 1,060,000 Atcon emails.
- Examination of the contents of 296 boxes of Atcon office documents (files, invoices, agreements, etc.) held in storage by the receiver.
- Examination of bank statements and cancelled cheques for the period of August 2007 to Atcon's bankruptcy date, with detailed testing of a sample of payments from July 2009 to bankruptcy, for all Atcon bank accounts (with some exceptions, discussed later).
- Review of Conflict of Interest Commissioner's 2013 report on allegations of conflict of interest by then Premier Shawn Graham, as well as 19 boxes containing transcripts and evidence presented during the investigation.
- Examination of court filings in connection with Atcon since it went into receivership.
- Examination of incorporating documents of Atcon group of companies as well as affiliated companies.
- Discussions with staff at Opportunities NB, the Office of the Attorney General and the Department of Transportation and Infrastructure.
- Interview of six Cabinet ministers involved in the 2009 decision to grant financial assistance to Atcon.
- Examination of electronic files on a hard drive received from the Progressive Conservative Party of NB.

2.32 We had access to the books and records of Atcon companies that were in the possession of one of the court appointed

receivers, Ernst and Young Inc. This included 856 boxes of documents held at a storage facility and Atcon computers located at a business office. We could not locate or access all the physical books and records for Atcon Industrial Services Ltd. (AIS) and Atcon Plywood Ltd (AP).

PricewaterhouseCoopers Inc. (PWC) was the court appointed receiver for these two companies. PWC responded as follows to our inquiries on the books and records of AIS and AP:

“At all times, these companies financial records were maintained at the corporate offices of the Atcon Group of Companies. Dormant Financial records were kept offsite in another property. Both of these properties were under the control and supervision of Ernst and Young Inc.”

2.33 Upon further inquiry with Ernst and Young Inc., we were told the following:

“EY acting in its capacity as the Court appointed Receiver of the Atcon Group of Companies has provided your office with full access to all information and documentation in our possession inclusive of the 800 plus boxes of materials (...)”

Scope limitation

2.34 Despite our best efforts and access to company records, we were unable to locate certain pieces of information. There were significant gaps in our evidence. The information that we could not locate or otherwise access included:

- Bank statements and cancelled cheques for Atcon Plywood and Atcon Industrial (fabrication) for the months of February 2008 to June 2009 and cancelled cheques for the period of July 2009 to March 2010.
- Bank statements for Atcon Industrial (machinery) for the period of February 2008 to June 2009. Cancelled cheques for Atcon Industrial (machinery) for the period of February 2008 to March 2010.
- Bank statements of one Atcon Holdings bank account for July 2009 to March 2010; all cancelled cheques for four Atcon Holdings bank accounts.
- Cancelled cheques of particular months for Atcon Logistics (Jan 2010), Atcon Quebec (Oct 2009 and Jan 2010), Atcon Veneer (Dec 2009), and Dycon Construction (Oct to Dec 2009, Feb 2010).
- Bank statements and cancelled cheques for OPI AB and Vanerply AB in Sweden.
- The audit file of the financial statement auditors of

Atcon.

If we had been able to examine this missing information, it may have impacted our findings and conclusions.

Restriction in use of report

2.35 This report is the product of the examination of a company that went into receivership approximately seven years ago in March 2010. **The analyses performed and the conclusions reached in this report are based on the information available to us at the date of this report, as described in paragraphs 2.31 and 2.34. Should new information be brought to our attention after the date of this report, we reserve the right to review and modify our analysis, findings and conclusions.** Certain sections of this report were vetted with individuals, departments, companies and organizations, where possible.

2.36 Some personal information has been included in this report. We have taken care to disclose the minimum amount of information necessary to enable readers to understand the findings and conclusions presented.

Follow the dollar

2.37 The focus of our 2015 audit was the events surrounding government's decision making process in granting financial assistance to Atcon in 2008 and 2009, as well as how to improve the performance of the Department of Economic Development (now Opportunities NB). This examination follows the funds once they are in the hands of Atcon, the funding recipient.

2.38 We focused on the \$63.4 million in financial assistance provided by the Province in 2008 and 2009. Exhibit 2.4 shows the history of financial assistance provided to the Atcon group of companies since 1993, and highlights the activity that we will focus on. We limited our examination to \$63.4 million in financial assistance (loan guarantees for \$13.4 million and \$50 million) made in 2008 and 2009 for the following reasons:

- These two items were the most recent;
- These two items were the most significant in amount; and
- These two items led to significant losses for the Province.

Exhibit 2.4 - Financial assistance granted to the Atcon group of companies by the Department of Economic Development between 1993 and 2009. Highlighted lines are the area of focus of this report.

Enterprise Name	Year	Type of Assistance	Amount	Outstanding Balance as at March 2016
Atcon Plywood Inc.	1993-1994	Loan	\$ 250,000	-
Atcon Plywood Inc.	1993-1994	Forgivable Loan	750,000	-
Atcon Plywood Inc.	1993-1994	Grant	1,608	-
Atcon Plywood Inc.	1995-1996	Grant	2,605	-
Eastwood	1996-1997	Loan	435,070	\$ 226,291
Atcon Plywood Inc.	1998-1999	Loan Guarantee	350,000	-
Arvin Special Machinery	2000-2001	Forgivable Loan	347,695	-
Atcon Plywood Inc.	2000-2001	Loan Guarantee	11,196	-
Atcon Plywood Inc.	2001-2002	Grant	4,364	-
Atcon Group	2002-2003	Grant	50,000	-
Atcon Plywood Inc.	2002-2003	Grant	4,026	-
Atcon Plywood Inc.	2003-2004	Loan Guarantee	643,780	683,642
Nutritec Inc.	2003-2004	Loan	100,000	-
Atcon Plywood Inc.	2004-2005	Loan	4,000,000	1,342,682
Nutritec Inc.	2007-2008	Loan	650,000	663,770
Atcon Industrial	2007-2008	Loan	3,250,000	3,386,513
Atcon Industrial	2007-2008	Forgivable Loan	3,060,000	
Atcon Holdings Inc.	2008-2009	Loan Guarantee	13,362,845	13,604,697
Atcon Holdings Inc.	2008-2009	Loan Guarantee	50,000,000	46,920,707
Total			\$ 77,273,189	\$ 66,828,302

Source: *Financial Assistance to Atcon Holdings Inc. and Industry*, Chapter 2, Exhibit 2.4, Volume 1, 2015 Report of the Auditor General of NB, March 2015 (figures updated for recoveries between 2014 and 2016)

2.39 In our 2015 report *Financial Assistance to Atcon Holdings Inc. and Industry*, we reported the total amount outstanding from the \$50 million guarantee as \$49,651,248. As shown in Exhibit 2.4, this amount has decreased to \$46,920,707, mainly as a result of \$2,724,416 that was recovered from the receiver during 2015-2016.

2.40 At the time of Atcon's bankruptcy, the Province had paid the Bank of Nova Scotia \$50 million as required under the guarantee agreement. We reviewed the disbursement reports

of the two bankruptcy trustees for the Atcon group of companies. The Bank also recovered additional funds during the bankruptcy proceedings as a result of the Province giving up its security in favour of the Bank.⁵ Exhibit 2.5 shows the Bank's total estimated recoveries. In total, it appears the Bank recovered 78% (\$77.2 million) of the amount it was owed by Atcon. The Province only recovered 4.5% (\$2.8 million) of \$63.4 million. Had Cabinet not given up the Province's security in favour of the Bank, the Province would have recovered significantly more than it actually did. We could not determine with precision the amount the Province would have recovered had it not given up its security in favour of the bank but it could have been in the range of an additional \$12-19 million.⁶

Exhibit 2.5 - Estimate of total amount recovered by Bank of Nova Scotia following Atcon's bankruptcy

Estimate of total amount recovered by Bank of Nova Scotia following Atcon's Bankruptcy	
Amount owed to Bank of Nova Scotia (from Preliminary List of Creditors)	\$ 99,221,661
<u>Less Recoveries:</u>	
Payment from Province of New Brunswick	(\$ 50,000,000)
Disbursements from Ernst & Young	(26,734,496)
Disbursement from PricewaterhouseCoopers	(494,145)
Total recoveries	(\$ 77,228,641)
Estimated net loss to the Bank of Nova Scotia	\$ 21,993,020

Source: 29th Report of the Receiver (Ernst & Young), June 4, 2015 and 2nd Report of the Receiver (PricewaterhouseCoopers) at July 6, 2010 and 7th Report of the Receiver (PricewaterhouseCoopers) at February 13, 2015, table created by AGNB

⁵ As a result of an amendment to the priority position with respect to security. In exchange for the amendment, the Bank provided additional credit of \$10 million to Atcon.

⁶ The calculation of the amount the Province could have recovered is complex. It involves the legal interpretation of several agreements, and the allocation of costs incurred during the bankruptcy process as well as several estimates and assumptions. At the time, Business New Brunswick estimated the loss from giving up security could have been up to \$19 million.

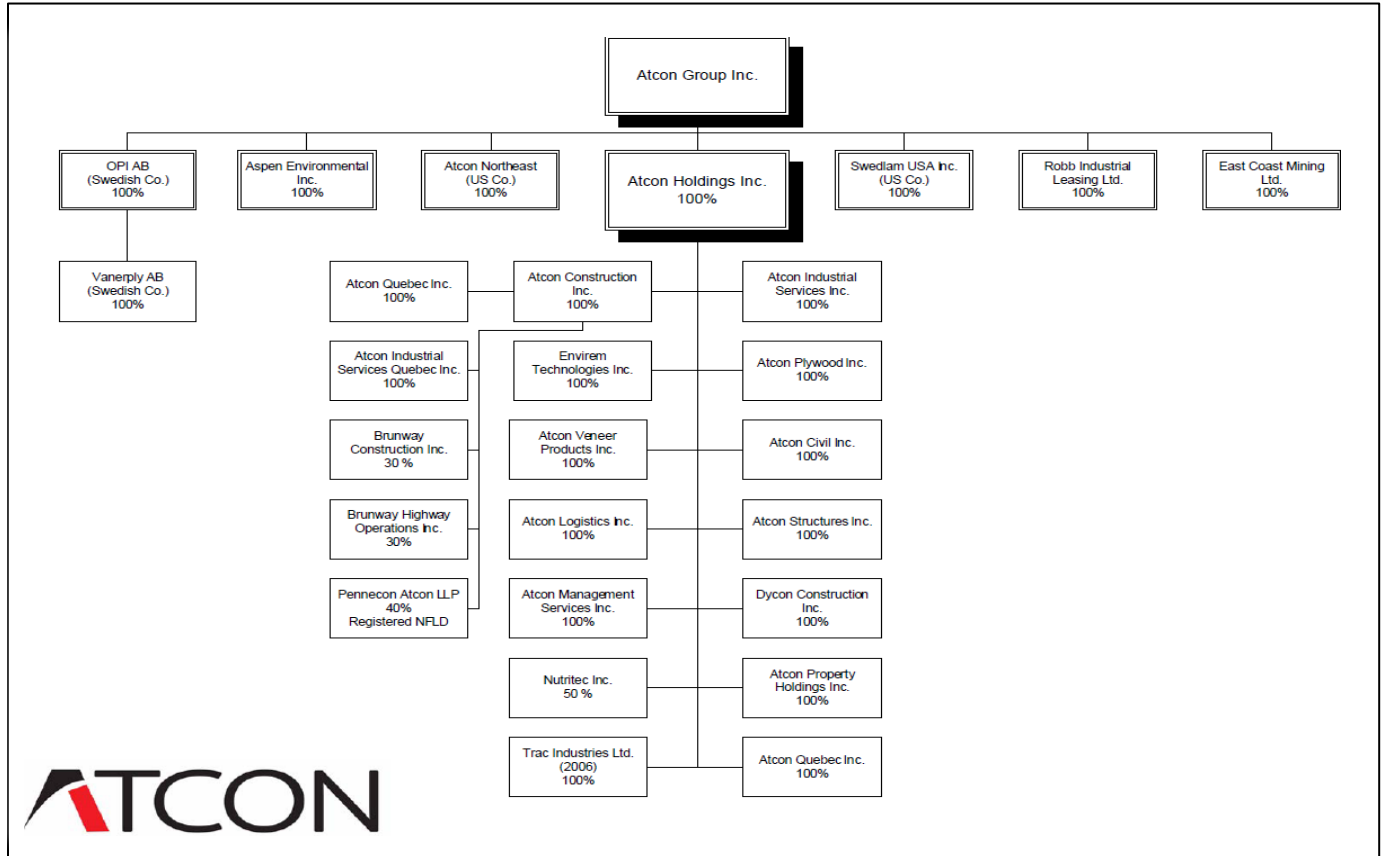
Financial assistance to Atcon

- 2.41** As seen in Exhibit 2.4, Atcon has received financial assistance from the Province on numerous occasions since 1993, including loans, forgivable loans, grants, and loan guarantees.
- 2.42** Beginning in 2008, the Province granted significant loan guarantees totaling \$63.4 million to Atcon Holdings Inc.
- In May 2008, the Province provided a guarantee of \$13.4 million for the purpose of securing a line of credit as required under the Deh Cho Bridge construction contract.
 - In June 2009, the Province provided a series of three loan guarantees to Atcon Holdings Inc. totalling \$50 million dollars for the purposes of completing an expansion of one of its facilities (\$10 million), replacing existing high interest debt (\$20 million) and to assist with working capital (\$20 million).
 - In March 2010, the Province was required to pay out the \$50 million guarantee. This was followed by a payout related to the \$13.4 million guarantee in October 2010, for a total of \$63.4 million.
- 2.43** As at March 31, 2016, almost \$67 million of financial assistance to Atcon companies remained uncollected by the Province. A timeline of key events can be found in Appendix I at the end of this report.

Atcon is a complex company

- 2.44** The Atcon Group Inc. was a New Brunswick company headquartered in Miramichi. Its activities included heavy civil construction, steel fabrication and machining, environmental products and services, and manufactured wood products. One of the difficulties we encountered in carrying out our work is the complexity of the Atcon organization. At the time Atcon received the \$50 million in financial assistance, its corporate structure consisted of 27 companies, all under the umbrella of Atcon Group Inc. Exhibit 2.6 shows the organization chart of the Atcon group of companies in 2008.

Exhibit 2.6 - Atcon group of companies in 2008



Source: 2008 corporate organization chart as found in Atcon's records.

Impact of 2008 economic slowdown on Atcon's activities

2.45 The economic crisis that began in 2008 may have contributed to Atcon's financial challenges as oil prices plummeted, projects were scaled back and financing opportunities became limited. We will examine Atcon's financial health later in this report.

Poor financial reporting practices

2.46 We also noted poor financial reporting practices during our examination of Atcon's books and records, which could have made monitoring the company's finances difficult. These included, for example, inconsistencies in year-end cut-off procedures, inconsistent treatment of commodity tax, and poor practices for managing and invoicing work in progress and change orders.

Costs incurred for unpaid work

2.47 Another issue that contributed to Atcon's financial challenges are costs incurred for work for which it was not reimbursed. During 2007 and 2008, Atcon was having difficulty collecting on claims it had submitted to Suncor⁷ and Canadian Natural Resources Ltd⁸ (CNRL) over unpaid amounts. Both of these accounts were subject to significant write-downs in the fall of 2009 totaling over \$19 million.

2.48 Atcon filed a lien in March 2009 for \$25 million in relation to work it was doing for Suncor on a project *Highway 63 Interchange*. Atcon made a claim for disputed change orders related to work performed between 2006 and 2008 for which it was not paid. The Atcon Advisory Board⁹ appears to have written-off \$11 million of this amount in November 2009. Settlement negotiations were held over the course of 2009, but the issue wasn't resolved until December 2010 when the receiver settled the outstanding balance for \$2.5 million¹⁰.

2.49 Atcon had change order requests with CNRL for \$34.7 million in mid-2008, for which the majority of work was performed in 2007. The Advisory Board appears to have written-off \$8 million of this amount in November 2009. We could not determine how much of the \$34.7 million balance was collected between 2007 and 2010 as we did not have the needed information. However, the receiver ultimately settled the outstanding balance for approximately \$216,000.¹¹

Unknown if issues were discussed with Province

2.50 Ultimately, the lack of timely collection of accounts receivable contributed to Atcon's failure. We cannot determine what level of detail concerning these accounts was shared with staff of Business New Brunswick prior to issuing financial assistance to Atcon, and whether it would have played a factor

⁷ Suncor is an integrated energy company whose operations include oil sands development and upgrading, onshore and offshore oil and gas production, petroleum refining and product marketing primarily under the Petro-Canada brand. (Suncor Energy Inc.'s 2015 annual report)

⁸ CNRL is an independent crude oil and natural gas exploration, development and production company. (CNRL's 2015 annual report)

⁹ As part of the conditions for the \$50 million guarantee, Atcon was required to arrange an Advisory Board acceptable to the Minister. The first meeting of the Advisory Board was in September 2009.

¹⁰ Per Receiver's Consolidated Statement of Receipts and Disbursements for the period of 1 March 2010 to 15 April 2015

¹¹ Per Receiver's Consolidated Statement of Receipts and Disbursements for the period of 1 March 2010 to 15 April 2015

in Cabinet's decision to provide financial assistance to Atcon.

Where Did the Money Go?

\$50 million

2.51 Atcon signed an agreement with the Province for three guarantees totalling \$50 million on June 30, 2009 in order to secure credit from its bank, the Bank of Nova Scotia. When Atcon defaulted on its loans in March 2010, the guarantees were called and the Province was required to pay \$50 million to the Bank of Nova Scotia. This is the simple answer to the question "where did the money go?" However, we wanted to know what Atcon did with the money that was subject to the guarantee prior to default.

2.52 Atcon received \$50 million in new loans from its bank through three deposits into one bank account:

- July 3, 2009: \$46 million
- July 17, 2009: \$2 million
- August 14, 2009: \$2 million

2.53 We examined the activity in Atcon's bank accounts, and reviewed other available documents, in order to determine what happened to the \$50 million received during the summer of 2009. We found \$24,324,077 was immediately paid to a law firm on July 3; these funds were then disbursed as detailed in Exhibit 2.7. The remainder of the \$50 million was used for various business expenses, also summarized in Exhibit 2.7. Our breakdown is based on documents found in the Atcon files.

Exhibit 2.7 - Use of funding by Atcon upon obtaining \$50 million guarantee from the Province

Use of funding by Atcon upon obtaining \$50 million guarantee from the Province		
Funding received by Atcon:		\$50,000,000
Amount transferred to law firm on July 3, 2009:		
Pay off high interest loans	\$ 21,391,491 ¹	
Pay out liens and judgments	1,239,729 ¹	
Pay outstanding property taxes	487,913 ¹	
Pay legal fees	454,944 ¹	
Amount put in trust to cover professional fees of consultants	<u>750,000¹</u>	(24,324,077)
Other amounts paid:		
Pay down operating line of credit at Bank of Nova Scotia	\$14,627,691 ²	
Bank of Nova Scotia fees	1,212,500 ²	
Remaining amount which appears to fund ongoing operations of Atcon (existing payables, lease payments, payroll, suppliers, etc.)	<u>9,835,732³</u>	(25,675,923)
		(\$ 50,000,000)

Source: financial records of Atcon Holdings Inc. including a statement of funds required for disbursement by law firm ⁽¹⁾ and Advisory Board information package of November 17, 2009. ⁽²⁾ The remaining amount ⁽³⁾ cannot be attributed to a single activity in line of credit account. Chart prepared by AGNB

Payments to NB suppliers

2.54 As shown in Exhibit 2.7, a significant portion of the money (\$14,627,691) was used to pay down the company's operating line of credit. Information found in the Atcon files suggests the company was over its borrowing base¹² on July 3, 2009, i.e. it was over its credit limit. At the deposit date, Atcon owed \$42,159,086 on its operating line of credit and had been given a temporary advance of \$1 million. The borrowing base¹³ at the time was calculated by Atcon to be \$28,531,395 which put Atcon \$14,627,691 over its borrowing base (or credit limit). As a result, it appears part of the \$50 million was used to pay down the company's operating line of credit and bring Atcon back within the terms of its borrowing base, but did not provide Atcon with additional working capital. Of the total funding of \$50 million, only \$9.8 million (approximately 20%) was

¹² The term "borrowing base" refers to the bank's approved credit limit based on Atcon's collateral assets.

¹³ Ibid.

actually new available credit.

2.55 One of the conditions of the guarantee agreements was for Atcon to pay all outstanding payables owed to New Brunswick companies. Atcon agreed to pay a total of \$6,532,381 to 314 NB suppliers, representing another use of the funds received in July 2009. The company provided a statutory declaration, signed by Atcon's Vice-President of Finance and Administration, stating Atcon had "authorized and caused to be paid those payments contemplated by and listed in my letter to Business New Brunswick dated June 11, 2009." The declaration was accompanied by a letter stating Atcon would "bring such payables current or within their respective credit terms within 10 business days of funding the proposed financing arrangements."

2.56 Based on our review, it appears Atcon released a number of cheques it had been holding for some time. Cheques were found clearing Atcon's bank account in July and August 2009 that had dates from late 2008 and early 2009. In some instances, the 2008 date had been crossed out and July 1, 2009 had been manually added, allowing the cheques to be processed.

2.57 We attempted to verify that the amounts owing to NB suppliers listed on the declaration had indeed been paid by Atcon as promised. During our search in Atcon's files, we did not find the supporting documents to match the declaration, such as invoices. Our analysis is based solely on the list of suppliers and amounts owed. We examined all available cheques and bank statements from July to September 2009 to determine how many of the amounts on the declaration had actually cleared the bank during the time period. We were able to identify 67 of 314 suppliers (21%) for whom cheques totaling \$1,180,942 were found clearing the bank which matched exactly to the declaration.

2.58 Though we could not match each and every supplier to a cancelled cheque, we were able to trace a number of amounts to cancelled cheques, as described in Exhibit 2.8. Exhibit 2.8 shows that 24 companies received payments greater than the amount listed on the declaration while 68 companies received less. For 155 companies, we found no cancelled cheques at all.

Exhibit 2.8 - Summary of cancelled cheque analysis: NB suppliers paid as per Atcon's declaration to Province of New Brunswick

Summary of cancelled cheque analysis: NB suppliers paid (between July and September 2009) as per Atcon's declaration to Province of New Brunswick			
Amount traced to cancelled cheque	Number of companies	Amount per declaration	Amount per cancelled cheques
Amount traced to a cancelled cheque is equal to amount on declaration	67	\$ 1,180,942	\$1,180,942
Amount on cancelled cheques is greater than amount on declaration	24	222,567	331,175
Amount on cancelled cheques is less than amount on declaration	68	2,882,125	1,414,946
No cancelled cheques found	155	2,246,746	-
Total	314	\$ 6,532,381	\$ 2,927,063

Source: Chart prepared by AGNB

2.59 For those companies where no cancelled cheque could be found, we compared the suppliers in question to certain Atcon payment registers (list of payments prepared) to determine if a cheque had been prepared for the amount listed on the declaration. We found cheques had been prepared for a large number of suppliers (some exact matches to the declaration, some over/under the amount on the declaration), but we also found 64 suppliers (owed a total of \$530,114 per the declaration) were not listed at all in the payment registers.

67 suppliers (21%) received the amount owed but we are unable to conclude on whether the remaining 247 NB suppliers received payment

2.60 We cannot determine with assurance, based on the information we have, that payment occurred or not for the following reasons:

- We were unable to trace all amounts on the declaration to a cancelled cheque;
- We did not have all cancelled cheques for all Atcon companies;¹⁴ and

¹⁴ As described in paragraphs 2.31 to 2.33, we could not locate the cancelled cheques of a number of Atcon accounts.

- Alternative explanations for payments may exist (such as a payment made through a trust account).

As a result, we can conclude that 67 suppliers (21%) received the amount they were owed (\$1.2 million) but we are unable to conclude whether the remaining 247 NB suppliers on the statutory declaration actually received payment.

Payments to suppliers, by province

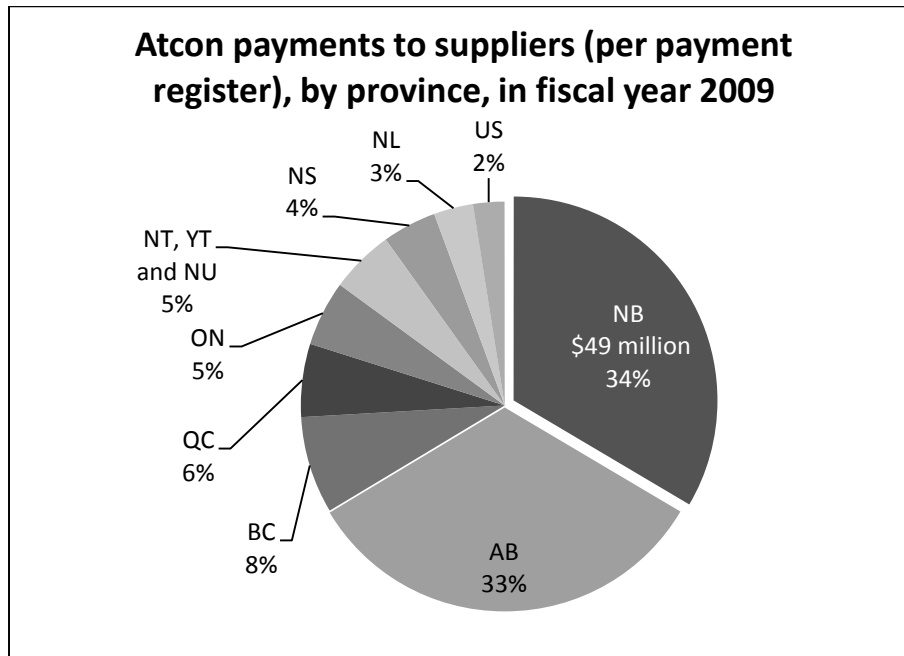
2.61 We analyzed Atcon's financial records to determine where some of Atcon's most significant suppliers were located and which vendors were paid. We examined the accounting records and payment registers of eight of Atcon's companies. These eight companies account for the vast majority of activity within the Atcon group of companies. The eight companies we examined are:

- Atcon Construction;
- Envirem Technologies;
- Atcon Industrial Services (fabrication);
- Atcon Industrial Services (machining);
- Atcon Management Services;
- Atcon Plywood;
- Dycon Construction; and
- Atcon Holdings.

2.62 For the year ended January 31, 2009 of these eight companies, Atcon had 1,446 suppliers with payments totaling just under \$148 million. Exhibit 2.9 shows for the year ended January 31, 2009, 33% (\$49 million) of amounts in Atcon's payment registers went to suppliers in New Brunswick¹⁵. It is important to note that Exhibit 2.9 is based on the payment registers only. We did not trace all payments to a cancelled cheque; therefore, we cannot conclude that suppliers actually received these payments.

¹⁵ NB supplier is determined based on telephone number (area code) listed in the vendor master file in Atcon's records.

Exhibit 2.9 - Atcon payments to suppliers (per payment register), by province, in fiscal year 2009



Source: payment registers to January 31, 2009 of eight Atcon companies (listed at paragraph 2.61), chart prepared by AGNB. NB supplier is determined based on telephone number (area code) listed in the vendor master file in Atcon's records. **Payments were not traced to cancelled cheques and therefore do not indicate actual payments received.**

2.63 We examined the payment registers for the amounts paid to NB suppliers. The average amount in the payment register to an NB supplier in 2009 was approximately \$65,000. We looked for suppliers who were listed above \$1 million and found nine NB suppliers over \$1 million in the payment registers. These suppliers included a number of steel fabricators, fuel distributors, asphalt and concrete companies, as well as construction equipment suppliers. We found nothing unusual in this list of suppliers.

2.64 We also looked at the payment registers for suppliers for the year ended January 31, 2010. During that period, Atcon had 1,026 suppliers with payments totaling just under \$33 million. At January 31, 2010, 37% of amounts in Atcon's payment registers were for suppliers in NB, at a value of \$12 million.

Largest ten Atcon suppliers

2.65 We also examined the activity for the ten largest Atcon suppliers in 2009. We found the top ten suppliers were paid (based on the payment registers) \$47 million for the year ended January 31, 2009. These suppliers included bridge contractors, fuel suppliers, heavy equipment rentals, steel fabricators and

trucking companies.

2.66 For the ten largest Atcon suppliers in 2010, the amounts per supplier were much smaller due a decrease in activity. The top ten suppliers were paid (based on the payment registers) \$10.6 million for the year ended January 31, 2010. The top ten suppliers included heavy equipment rentals, bridge contractors, structural steel erectors, oil and gas services, insurance and sandblasting.

Detailed testing

2.67 In addition to our detailed review of Atcon's banking activity, we also examined all cheques cashed between August 2007 and March 2010 (with exception of those noted in paragraph 2.34). Further, we selected a sample of cheques cashed between July 2009 and March 2010 for detailed analysis. We selected items over \$1,000 that appeared unusual, such as:

- high dollar or unusual amount;
- sequential cheques to the same vendor;
- unusual payee; and
- transfer of funds to companies outside the Atcon corporate group.

2.68 We attempted to trace all sample items to supporting documents, such as invoices. We tested a total of 110 items valued at close to \$28.5 million. We were able to trace 71% of our sample items to supporting documentation. We could not find supporting documentation for 29% of our sample items, which represented \$25.6 million in payments, but we concluded the vendor to whom the payment was made is a known vendor and appears plausible as an Atcon supplier.

Conclusion

2.69 Although certain supporting documentation could not be located for some of the cheques issued, it is our conclusion that the expenses we tested appear to be for business activities.

2.70 Overall, based on our analysis of the movement of the funds once they were in Atcon's control, we found the funds appear to have been largely used for business related activities and testing of cheques between July 2009 and March 2010 did not show any unusual or large payments to owners of Atcon or companies Atcon is known to control.

Where Did the Money Go?**\$13.4 million***Description of bridge issues*

- 2.71** On May 29, 2008, Atcon received a loan guarantee for \$13,362,845 from the Province in order to secure a Letter of Credit from its bank, as required under a \$133,628,450 bridge construction contract in the Northwest Territories. The purpose of the letter of credit is to secure performance obligations related to the construction of the bridge, at an amount of 10% of the total contract value.
- 2.72** Work on the bridge began in June 2008. In 2009, the design of the bridge was reviewed and the Deh Cho Bridge Corporation determined the current design of the bridge did not meet Canadian Highway Bridge Design Code standards. Negotiations with Atcon for a revised price, term and project schedule as a result of the redesign were not successful. Atcon was notified it was terminated from the bridge contract in December 2009.
- 2.73** As the bridge contract was terminated at the end of 2009, Atcon's bank decided to not renew the letter of credit, set to expire on November 1, 2010. The Government of Northwest Territories (GNWT) advised the Province there were deficiencies in the construction of the bridge by Atcon, and funds would be needed to address the deficiencies. As a result, on October 27, 2010, the Province agreed to pay the GNWT an amount of \$13,362,845. The Deh Cho Bridge officially opened on November 30, 2012.
- 2.74** In its agreement with the Province, the GNWT was to deposit the \$13.4 million into an interest bearing account and withdraw from the account only to pay or reimburse itself for:
- Costs of identifying and remedying any deficiencies related to the work performed (or required) by Atcon or its contractors/subcontractors under the Deh Cho contract;
 - Costs of any defaults by Atcon, its contractors or subcontractors under the Deh Cho contract;
 - Amounts otherwise owing under the Deh Cho contract by Atcon; and
 - Legal and other costs incurred by GNWT associated with the negotiation, execution, performance and enforcement of the agreement.
- 2.75** In return for the funds, the GNWT was to provide the Province with an accounting of the costs, along with supporting documents. Any surplus funds in the account were to be

returned to the Province within six months following the final rectification of the deficiencies.

2.76 We contacted Opportunities NB (ONB) to determine the current status of the \$13.4 million payment and examine the correspondence between GNWT and the Province to ensure the payment was properly supported. Based on information provided to us by ONB, there was intermittent quarterly reporting from GNWT on the status of the funds; we noted large gaps of time where it appears there was no reporting. ONB indicated to us it did not always require quarterly statements. The GNWT indicated there was no need to report when there was no work performed or expenditures incurred, resulting in the gaps we observed.

ONB obtained support for \$13.4 million payment to GNWT six years after payment

ONB has not completed its review of GNWT support for payment

2.77 We also learned ONB requested supporting documents for the \$13.4 million in a letter to the GNWT in February 2016, some six years after the money was provided to GNWT. In July 2016, GNWT provided ONB with a report on deficiencies and costs. We examined the report, which indicates the cost to identify and remediate the deficiencies, in addition to legal and other anticipated cost, is in excess of \$14 million. Supporting documents have been made available to ONB, but at the time of our examination, ONB had not yet completed its review of the documents provided. Based on the information provided by GNWT, there are no surplus funds remaining following the rectification of deficiencies on the bridge attributable to Atcon. Because ONB had not yet completed its review of the support provided by GNWT, we were unable to confirm that the payment to GNWT was supported by documents and analysis.

2.78 ONB has indicated to us the request for supporting documents from GNWT was made in 2016 for the following reason:

“The claimed costs by the GNWT were not fully finalized until March 31, 2015 and the final Summary Status Report received until October 2015. Once the final Summary Status Report was received, it was reviewed by ONB. (...) A formal request letter was sent in February 2016 to GNWT requesting all available documentation and backups to fully substantiate the \$13.3M per the Agreement.”

2.79 ONB has also indicated the review of the supporting documents received was not completed at the time of our examination because:

“The August 2016 document package provided by GNWT

was not complete (...). As soon as it was recognized that the July/August 2016 information provided was not adequate, additional requests were made in November 2016 to provide all supporting documentation. (...) Partial documentation was provided in December 2016 and January/February 2017 by GNWT. GNWT has indicated there are approximately 20 boxes of information to be scanned in total. Staff at ONB is currently reviewing the information received by GNWT. The review is not complete at this point, but potential next steps have already been identified.”

Recommendation 2.80 We recommend, for performance bonds or funds placed in trust, Opportunities NB structure the release of such funds such that sufficient supporting documentation is obtained and reviewed for authenticity and legitimacy prior to authorizing the disbursement of funds.

Questionable personal benefit 2.81 We decided to examine the activity on company credit cards, as well as in the shareholder account. In our review of Atcon’ records, Atcon used a shareholder account to identify moneys paid by the company on behalf of a shareholder. At certain intervals, companies using a shareholder account in this way would normally declare dividends (pay the shareholder additional remuneration) to clear or reduce the shareholder account. This ensures the shareholder recognizes “income” received by means of personal expenses paid by the company. While we understand this may be a normal practice for some companies, we found it questionable to do so if there are large amounts of personal expenses paid by a company while applying for significant financial assistance from the Province.

Personal expenses paid through company accounts 2.82 We found that certain individuals put personal expenses through company accounts totalling close to \$735,000 during the years ended January 31, 2008 to January 31, 2010, as detailed in Exhibit 2.10.

Exhibit 2.10 - Personal expenses paid through Atcon accounts, during the years ended January 31, 2008 to January 31, 2010.

Personal expenses paid through Atcon accounts, during the years ended January 31, 2008 to January 31, 2010	
Credit card charges deemed personal in nature	\$29,354
Amounts charged to the Shareholder’s Account	\$705,635
Total	\$734,989

Source: financial records of Atcon Holdings Inc., chart prepared by AGNB.

Credit card activity 2.83 We reviewed a sample of credit card activity as well as activity in the shareholder account during the years ended January 31, 2008 to January 31, 2010 when Atcon was seeking or received significant financial assistance from the Province. The purchases during these periods are shown in Exhibits 2.11 to 2.13. Not all credit card statements during this period were available to us as we could not locate all the statements. We cannot determine with complete assurance that the expenses noted in the following exhibits are of a personal nature. We used our best judgment based on other evidence we came across during our work, such as emails or other corroborating documents. The credit cards we examined are for the shareholder of Atcon, or his spouse, as well as a corporate travel card.

Exhibit 2.11 - Purchases made in the year ended January 31, 2008 by shareholder when Atcon was seeking financial assistance from the Province.

Purchases made in the year ended January 31, 2008 by shareholder when Atcon was seeking financial assistance from the Province	
Purchase	Amount
Luxury car lease payments	\$ 14,647
Annual RRSP contribution of shareholder/family	28,253
Jewelry	15,006
Vacation property in Aruba	57,253
Two properties in NB	60,132
Shares and property in a New Brunswick company	137,394
Personal income taxes	12,845
Property taxes	10,679
Other activity identified as personal	74,934
	\$ 411,143

Source: financial records of Atcon Holdings Inc., chart prepared by AGNB.

Exhibit 2.12 - Purchases made in the year ended January 31, 2009 by shareholder when Atcon was seeking financial assistance from the Province.

Purchases made in the year ended January 31, 2009 by shareholder when Atcon was seeking financial assistance from the Province	
Purchase	Amount
Luxury car lease payments	\$ 14,518
Annual RRSP contribution of shareholder/family	38,000
Personal income taxes	100,265
Property taxes	15,151
Other activity identified as personal	38,359
	\$ 206,293

Source: financial records of Atcon Holdings Inc., chart prepared by AGNB.

Exhibit 2.13 - Purchases made in the year ended January 31, 2010 by shareholder when Atcon was seeking financial assistance from the Province.

Purchases made in the year ended January 31, 2010 by shareholder when Atcon was seeking financial assistance from the Province	
Purchase	Amount
Luxury car lease payments	\$ 8,469
Annual RRSP contribution of shareholder/family	50,000
Property taxes	16,193
Payment on personal line of credit	5,000
Other activity identified as personal	8,536
	\$ 88,198

Source: financial records of Atcon Holdings Inc., chart prepared by AGNB.

2.84 Dividends to the shareholder of \$250,000 in 2007 and \$265,000 in 2008 (totalling \$515,000) were noted in the files of Atcon. When a dividend is paid out, it allows the company to offset the personal benefit to the shareholder, as the shareholder is then required to include the dividend in their taxable income. However, only the dividend of \$265,000 was recorded in the general ledger of Atcon; as a result, we are not certain the \$250,000 dividend was actually declared. In addition, we did not have access to the taxation files of the individuals involved; therefore, we cannot determine whether the dividends, if declared, were actually included in the income of the individuals involved or if there were other dividends in excess of what we found in the records reviewed.

2.85 The loan guarantee agreement signed by Atcon does place restrictions on declaring dividends when the dividends are not in the normal course of business. We did not determine whether the dividends discussed above were “in the normal course of business”. It is our opinion that such dividend payments were inappropriate given the significant amount of financial assistance the Province was providing at the time.

Corporate jet costs over \$2 million per year

2.86 Atcon had a corporate jet at the time it requested the \$50 million guarantee from the Province. Atcon began leasing the aircraft in early 2007 at a cost of \$123,925 (plus applicable taxes) per month. The aircraft had a seating capacity of 20

people.

2.87 Based on the documents we examined, it appears Atcon made some effort to dispose of or sublease the aircraft after receiving the guarantee from the Province. In September 2009, it arranged to “dry lease¹⁶” the aircraft to a company in Quebec.

2.88 We were surprised to find a company under significant financial pressure, coming to the Province for financial assistance, would have an item as extravagant as a corporate jet. The Province was aware of the existence of the jet, as noted in the commentary on a request for assistance dated March 13, 2009 that states “*the recent acquisition (by lease) of a corporate jet will create a perception issue if assistance is provided.*” We examined the costs associated with operating the jet using Atcon’s trial balances for the years ended January 31, 2008 to January 31, 2010. We estimate the direct costs of operating the jet during the three years examined was almost \$8.2 million. Our findings are detailed in Exhibit 2.14.

Exhibit 2.14 - Estimate of costs to operate Atcon’s corporate jet for the years ended January 31, 2008 to January 31, 2010

Estimate of costs to operate Atcon’s corporate jet for the years ended January 31, 2008 to January 31, 2010				
	Year ended			Total
	2008	2009	2010	
Expenses	\$ 2,795,169	\$ 3,028,776	\$ 2,355,316	\$ 8,179,260

Source: financial records of Atcon Logistics, chart created by AGNB

2.89 We found correspondence pertaining to a potential taxable benefit for the personal use of the aircraft by the owner of the company, but we could not determine if such a benefit was ever calculated. We examined flight schedule spreadsheets, prepared by staff of Atcon, for unusual use of the aircraft. The schedules were for 129 flights between February 2007 and July 2009. The schedules identify the date of the flight, the departure location and destination, as well as the names of

¹⁶ “Dry lease” refers to the leasing of an aircraft without crew, maintenance or fuel.

passengers on the aircraft. The aircraft flew mainly to areas such as Fort McMurray, Calgary and Toronto, and passengers were typically the shareholder, executive staff and construction staff of Atcon. Unusual use could be a combination of who is on the plane and the destination and whether the flight was for business or personal reasons. Of the 129 flights schedules reviewed, we identified 9 flights that appeared to be of a personal nature based on the passenger list. We were unable to quantify the personal benefit received from the use of the aircraft because we didn't have the information needed to do so.

Management payroll and compensation

2.90 We examined the compensation, in addition to amounts from the shareholder account, paid to key management staff at Atcon for the years 2007-2010, as well as expense claims. We looked at this information to determine if there were any unusual payments indicating an inappropriate benefit to key management staff.

2.91 The three key management staff received compensation, in total for the group (in addition to personal expenses and dividends mentioned earlier), ranging between \$554,000 and \$603,000 annually between 2007 and 2009¹⁷. We also found there were annual increases of 4% to 5% in total compensation paid to these three key members of senior management between the years 2007 and 2009. Though compensation increased during the period when Atcon received significant financial assistance from the Province, the increase was not significant enough, in our view, to indicate an inappropriate benefit.

2.92 We also examined the compensation to family members of key management staff. Total annual compensation to this group of individuals ranged between approximately \$340,000 and \$378,000 between 2007 and 2009. For some of these individuals, we found little evidence they did any work for Atcon. We considered some of the compensation paid to family members as significant, given their apparent limited or lack of involvement in the day-to-day operations of the company.

¹⁷ 2010 is not included as some key members left Atcon in 2010

2.93 In reviewing salary payments to key senior management, we did not find any payments that were excessive or would be classified as unusual, with the exception of payments to certain family members who did not appear to have a regular and sustained presence at Atcon.

Expense claims

2.94 We also examined expense claims for the calendar years 2008 and 2009 for key management staff. We found no unreasonable amounts in our examination.

**Atcon's
Financial
Health: Cash
Flow Problems**

2.95 Atcon was operating under significant cash flow stress in 2009. We found numerous emails from suppliers, as well as emails within the company itself, describing a corporate environment with severe cash flow problems. Our review of emails identified the following issues:

- Poor project management practices which lead to higher project costs;
- Poor costs control on jobs;
- Bounced cheques to suppliers;
- Cheques not issued due to lack of funds; and
- Contractors and suppliers unable to receive payment from Atcon.

**In-depth analysis
of Atcon's
financial
statements**

2.96 We performed an in-depth analysis of Atcon Holdings's financial statements and financial records in order to gain a better understanding of the company's financial status before it received the \$50 million guarantee from the Province in June 2009.

2.97 During our analysis, we noted two significant but related irregularities in the audited financial statements of Atcon Holdings at January 31, 2009:

- Discrepancy of \$23 million between the balance sheet and the statement of cash flow; and
- Questionable reclassification of \$21.7 million (in short term accounts payable to long term liabilities).

*Discrepancy
between balance
sheet and statement
of cash flow of
Atcon's audited
financial statements*

2.98 When we examined the January 31, 2009 audited financial statements of Atcon, we noted the statement of cash flow indicated an increase in the Accounts Payable and Accruals line of \$16,270,402. However, the balance sheet showed a decrease of \$6,682,726 in this line item. This difference in presentation amounts to a discrepancy of \$22,953,128. The discrepancy appears to be due largely in part to the

reclassification of a portion of trade payables and accruals from current to long term. The reclassification was made on the balance sheet, but not carried over to the cash flow statement. Had the reclassification been carried over to the cash flow statement, it would have showed negative cash flow instead of positive cash flows from operations (previous years statements show negative cash flows from operations).

2.99 A statement of cash flow is a key financial statement that shows the amount of cash received and spent by a company. It can be used to identify business performance trends that are not readily apparent in the rest of the financial statements.

Questionable reclassification of accounts payable improves (in appearance) the financial condition of Atcon

2.100 Based on our review, Atcon would have been unable to continue normal operations due to its deteriorating financial position. At its January 31, 2009 year end, the company was in violation of its debt covenants and it owed more to its suppliers than it could pay from its financial resources.

2.101 A “subsequent event” note in the financial statements at January 31, 2009 states Atcon’s ability to continue operations is dependent upon getting new financing in place, maintaining its borrowing base and meeting the revised debt covenants. The “subsequent event” note was added as of June 18, 2009 (the financial statements are dated May 7, 2009, except for this note.) The note included a late change made to the financial statements. It stated “*The Company has reclassified \$21.7 million of its payables and accruals at January 31, 2009 to reflect the working capital and term funding received in the new credit facility.*”

2.102 This adjustment reduced the amount shown on the financial statements as owing to suppliers at January 31, 2009 and added it to long term liabilities. The purpose of the adjustment is to show the *anticipated* effect of the new (government guaranteed) financing secured five months after year end on June 30, 2009. According to the financial statement note and reclassification adjustment, the new financing was going to be used to pay off amounts owing to suppliers at year end; this would improve the short term health and liquidity of Atcon, allowing the financial statements to remain on a going concern

basis¹⁸.

2.103 At the January 31, 2009 year end, Atcon owed \$63 million to suppliers; following the reclassification, the amount recorded on the payables and accruals line of the balance sheet showed only \$41 million owed. The adjustment to the financial statements gave the appearance that over \$20 million was going to be used to pay off suppliers. However, we found most of the new \$50 million in financing was used to pay off the line of credit and other debt and refinancing costs, leaving less than \$10 million available to pay amounts owed to suppliers. As a result, we find the June 2009 reclassification of \$21.7 million to the balance sheet appears questionable.

2.104 We also found the reclassification improved the financial position of the company, at least in appearance. The reclassification artificially improved Atcon's current ratio, a key measure used to assess the liquidity and credit worthiness of a company. Before reclassification, Atcon's current ratio was less than 1; after the reclassification, it increased to 1.21, as shown in Exhibit 2.15. A current ratio that is less than 1 indicates the amount owed in the short term exceeds the company's ability to pay. Therefore, the reclassification improved the financial position (in appearance) of Atcon at January 31, 2009.

Exhibit 2.15 - Current ratio of Atcon Holdings Inc. before and after reclassification at January 31, 2009 year end

Current ratio (current assets / current liabilities) of Atcon Holdings Inc. before and after reclassification at January 31, 2009 year end			
	Before reclassification	Reclassification	Audited balance sheet (after reclassification)
Current assets	\$ 116,255,252		\$ 116,255,252
Current liabilities	\$ 118,274,581	(\$ 21,700,000) *	\$ 96,035,752
Current ratio	0.99		1.21

*The discrepancy found is greater than the \$21.7 million amount actually shown. Since we were unable to reconcile the amount, we are using the value identified in note 19 to the consolidated financial statements of Atcon Holdings Inc. at January 31, 2009.

Source: 2009 audited consolidated financial statements of Atcon Holdings Inc. Chart prepared by AGNB

¹⁸ The going concern assumption is an accounting principle that requires companies to be accounted for as if they will continue operating in the future, or in other words, as if the company is not expected to fail. (from www.myaccountingcourse.com)

2.105 Since such a large amount of current trade payables was reclassified as long term, we expected to see a number of items, totalling \$21.7 million, specifically identified and set aside in the financial records of Atcon for payment from the proceeds of the new financing.

2.106 We inspected the accounts payable reports and accruals we found in Atcon's accounting records; we found no support in the financial records for the reclassification. Ultimately, we were unable to identify any accounts payable or accruals that were actually reclassified (or separately identified for refinancing to long term) in the accounting records of Atcon we had access to.

2.107 To obtain an explanation, we requested access to the January 31, 2009 financial audit file from the auditors of Atcon, who responded through their legal counsel as follows:

In order that we may assess your request for access to Grant Thornton's file in relation to the audit of Atcon Holdings Inc. for the year ended January 31, 2009 and provide you with an informed response, would you please clarify exactly what information from the audit file you are seeking to examine as we believe the information in the file will be of no benefit to you given our understanding of your current mandate. Further, we would also request that you confirm under which provisions of the performance audit provisions of section 9.1(2) the Auditor General Act you are proceeding.

Given this response, as well as the fact there is pending litigation between the Province and Grant Thornton, we opted to not pursue this issue further.

Financial analysis identifies serious concerns

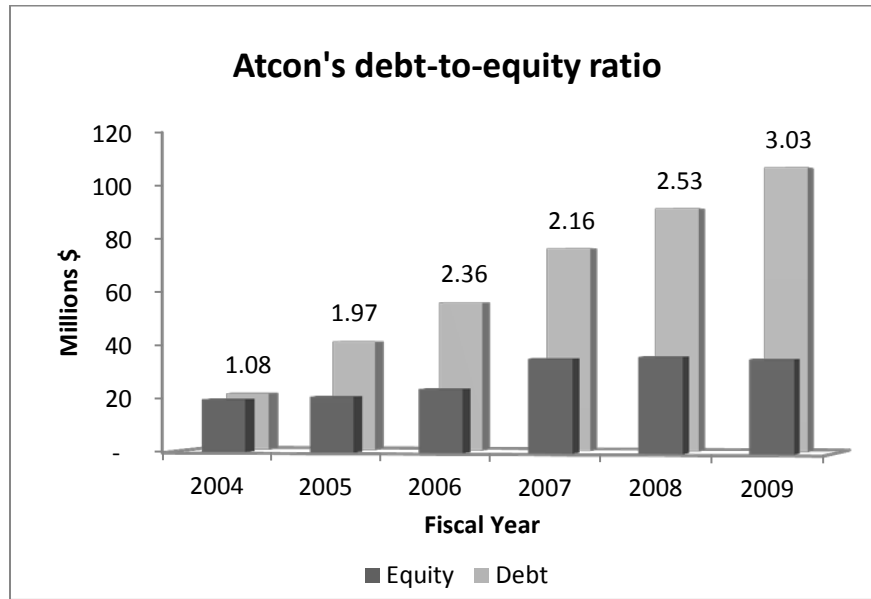
2.108 We performed an extensive analysis of the consolidated audited financial statements of Atcon. We examined information for the fiscal years ended January 31, 2004 to January 31, 2009, looking for trends in key areas to gain an understanding of Atcon's financial health. Our analysis shows a company with a growing amount of debt, insufficient working capital and a severe cash shortage.

Growing debt-to-equity ratio

2.109 Atcon was rapidly becoming highly leveraged in the years leading up to 2009. That is, an increasingly large share of the company's value and assets were coming from debt financing rather than shareholder equity, as shown in Exhibit 2.16. A growing company that is healthy and profitable should be adding or accumulating equity. Equity is the difference

between the value of a company's assets and its liabilities, and represents the net value of a company. In Atcon's case, growth was being funded by creditors. Between 2004 and 2009, Atcon's debt-to-equity ratio tripled from 1.08 to 3.03.

Exhibit 2.16 - Atcon's debt-to-equity ratio, fiscal years 2004 to 2009



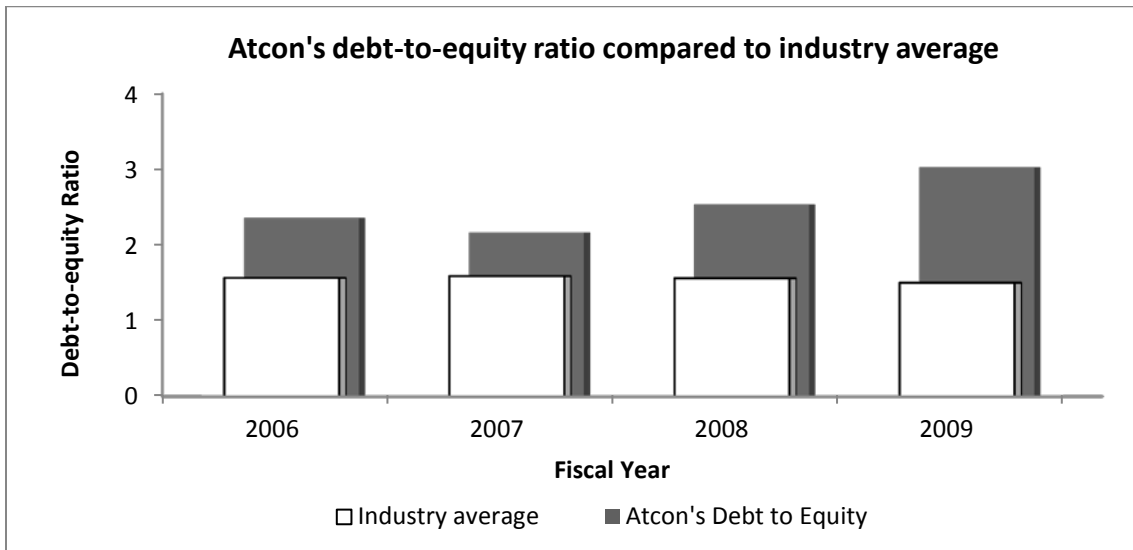
Source: audited consolidated financial statements of Atcon Holdings Inc., chart prepared by AGNB

Atcon's debt-to-equity ratio was double the industry average

2.110 Next, we compared Atcon's debt-to-equity ratio to the industry average. In Exhibit 2.17, we can see that Atcon's debt-to-equity ratio is much higher than its industry average¹⁹, meaning Atcon had much more debt as compared to equity than the industry norm, and there is less residual value in the company. In 2009, Atcon's debt-to-equity ratio was double the industry average.

¹⁹ Industry average from Statistics Canada Cansim tables

Exhibit 2.17 - Atcon's debt-to-equity ratio compared to industry average, fiscal years 2004 to 2009



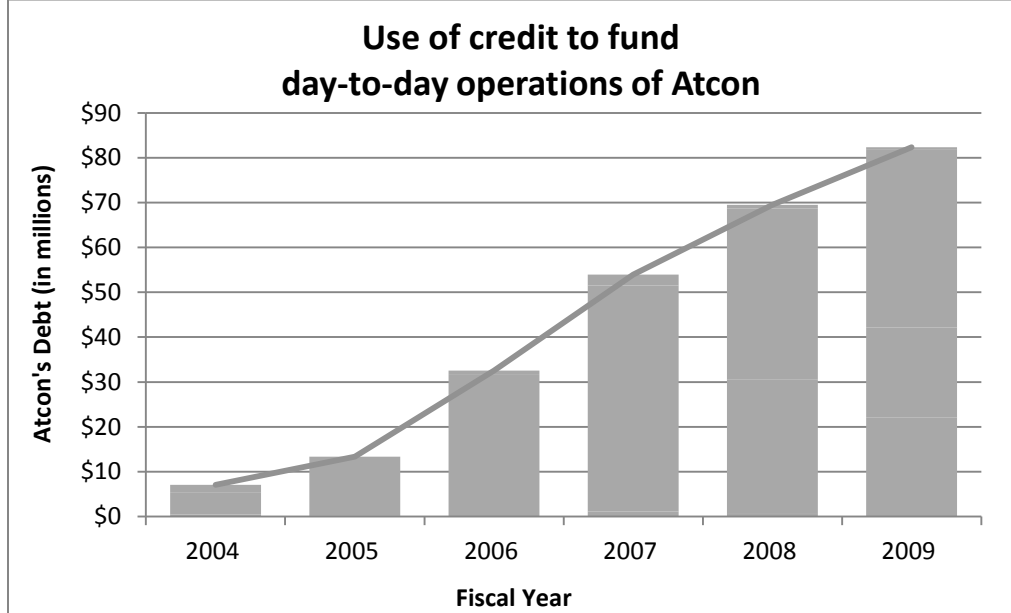
Source: audited consolidated financial statements of Atcon Holdings Inc., industry average from Statistics Canada Cansim tables, chart prepared by AGNB

Growing use of debt to fund operations

2.111 We also looked at how Atcon was using its debt. We expected to see debt being used to buy tangible assets, such as equipment or machinery, which can be used to earn profits for the company. Instead, we found Atcon was increasingly using debt to fund its day-to-day operations, as shown in Exhibit 2.18. Atcon's debt is made up of lines of credit, bank indebtedness (amounts owing to a bank, akin to bank overdraft), subordinated debt²⁰ (loans) and long term liabilities (obligations that are not due in the next 12 months). As shown in Exhibit 2.16, Atcon had total debt of \$107 million in 2009; over \$80 million (75%) of this debt was used for working capital. In simple terms, this is like using mortgage proceeds to buy groceries.

²⁰ Subordinated debt refers to a loan that ranks after other debts if a company falls into bankruptcy.

Exhibit 2.18 - Use of credit to fund day-to-day operations of Atcon



Source: audited consolidated financial statements of Atcon Holdings Inc., chart prepared by AGNB

Severe cash shortage

2.112 In 2007, we noted the company had a severe cash shortage prompting them to access funds in the form of high interest subordinated debt²¹. Exhibit 2.19 shows the company was consistently and increasingly in a negative cash position from 2004 to 2009.

Exhibit 2.19 - Atcon's net cash position at January 31, 2004 to 2009 (in millions)

Atcon's net cash position at January 31, 2004 to 2009 (in millions)						
Net cash position at Jan 31	2004	2005	2006	2007	2008	2009
	(\$ 6.5)	(\$ 13.1)	(\$ 15.5)	(\$ 22.4)	(\$ 38.6)	(\$ 40.2)

Source: audited consolidated financial statements of Atcon Holdings Inc., chart prepared by AGNB

Insufficient resources to fund operations

2.113 We looked at Atcon's working capital as a key measure of solvency. Solvency is a company's ability to pay its debts as they become due²². Examining the components of working capital over time can provide us with a very good indicator of

²¹ Subordinated debt refers to a loan that ranks after other debts if a company falls into bankruptcy.

²² www.investinganswers.com

the financial health of Atcon.

2.114 Working capital turnover measures how well a company is using its working capital to support a given level of sales.

Atcon's working capital turnover is displayed in Exhibit 2.20.

Exhibit 2.20 - Atcon's working capital turnover ratio, January 31, 2004 to 2009, compared to industry average

Atcon's working capital turnover ratio at January 31, 2004 to 2009, compared to industry average							
Fiscal Year	2004	2005	2006	2007	2008	2009	2009 Before Reclassification
Atcon's working capital turnover	9	30	17	44	37	22	807
Industry Average	n/a ¹	n/a ¹	4	4	4	3	3

¹ Data was not available

Source: audited consolidated financial statements of Atcon Holdings Inc., industry average from Statistics Canada Cansim tables, chart prepared by AGNB

2.115 As seen in Exhibit 2.20, when compared to industry average, Atcon's working capital turnover ratio is very high between 2007 and 2009. Once we remove the effect of the reclassification of accounts payable, the ratio for 2009 increases dramatically to 807. An extremely high working capital turnover ratio can indicate a company does not have enough capital to support its sales growth, and collapse of the company may be imminent²³. This is a particularly strong indicator when the accounts payable component of working capital is very high, since it indicates that management cannot pay its bills as they are due.²⁴

Overall analysis on debt position **2.116** Our overall analysis indicates the company's main source of cash was financing or debt. Based on the results of our trend analysis from 2007 to 2009, there is a strong indication it was unlikely the company would have had the ability to repay its

²³ www.accountingtools.com/working-capital-turnover-ratio

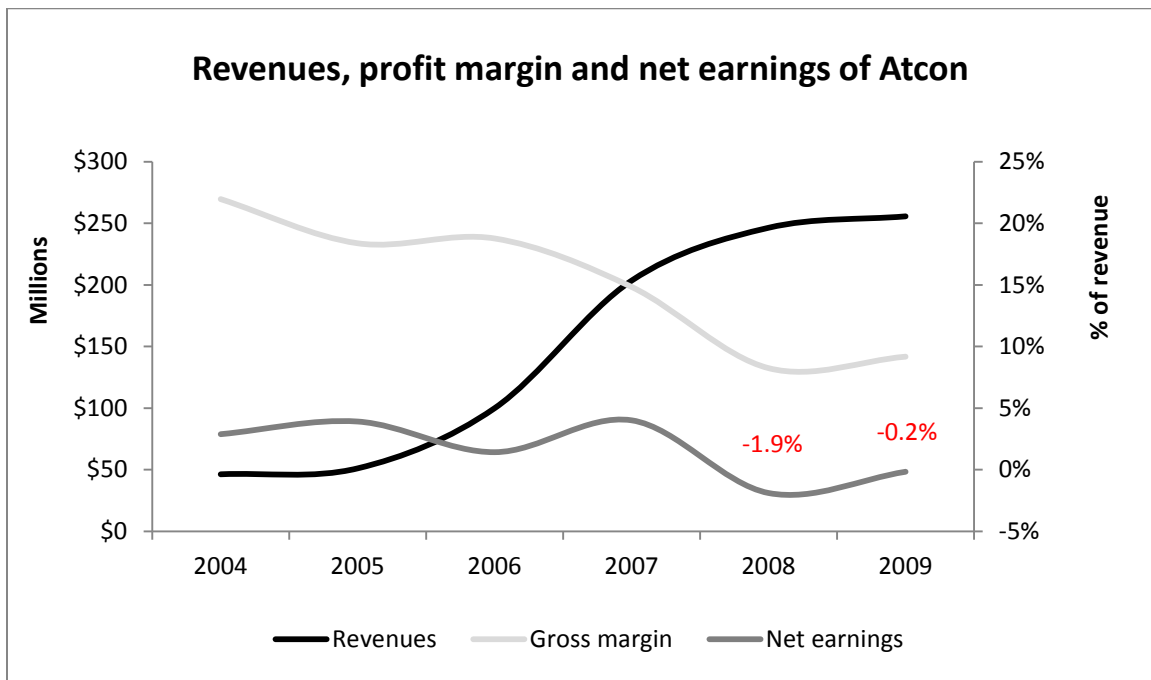
²⁴ Ibid

debt because cash from operations was consistently negative. In other words, Atcon was not making enough money to pay its current bills, let alone pay down its existing or future debt. In addition, Atcon did not have the working capital needed to support its increased volume of business. As debt was being used to cover its working capital shortfall, it was not being used to invest in long term initiatives which could generate future revenue.

Growth from low quality revenue

2.117 We also looked at Atcon's revenues during the period of 2004 to 2009. As shown in Exhibit 2.21, revenues increased significantly between 2005 and 2009, but the profit margin was decreasing, going from 22% in 2004 to 9% in 2009. Though total revenue increased from \$46 million in 2004 to \$256 million in 2009, net earnings were decreasing. As a result, Atcon was doing more work but earning proportionately less profit.

Exhibit 2.21 - Revenues, profit margin and net earnings of Atcon from 2004 to 2009



Source: audited consolidated financial statements of Atcon Holdings Inc., chart prepared by AGNB

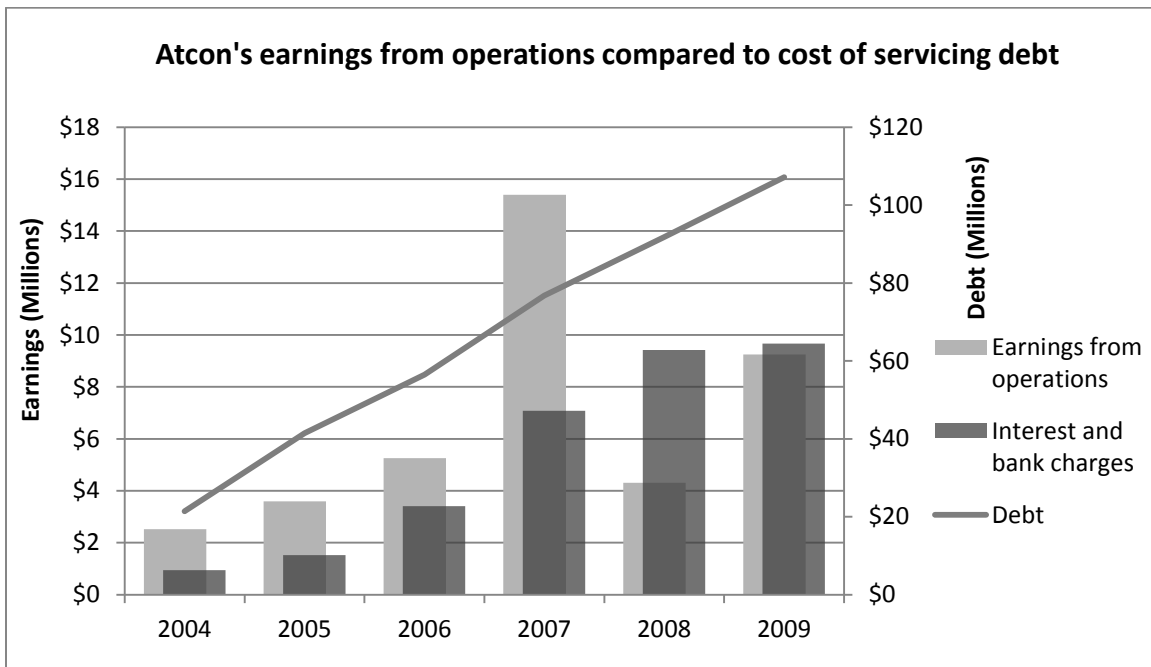
Debt spiral

2.118 Our analysis indicates Atcon was caught in a debt spiral. Atcon made up for its cash shortfall from operations by borrowing cash, first from its Bank of Nova Scotia approved overdraft then from its Bank of Nova Scotia line of credit. The continuing cash shortfall caused Atcon to resort to high interest

subordinated debt²⁵ for financing. As cash used to pay interest and principal payments on this “high cost” debt can’t be used to fund day-to-day operations, it created an additional cash shortage. This additional cash shortage caused Atcon to borrow more money, putting further strain on future cash flows required to service and pay off debt, and further limiting cash available for day-to-day operations.

2.119 As Atcon’s debt continued to grow, interest and bank charges began outpacing earnings from operations in 2008 and 2009, as shown in Exhibit 2.22, taking an increasingly larger bite out of earnings and further exacerbating Atcon’s cash problems. In 2009, Atcon’s earnings from operations of \$9.3 million were outpaced by interest and bank charges of \$9.7 million.

Exhibit 2.22 - Atcon’s earnings from operations compared to cost of servicing debt



Source: audited consolidated financial statements of Atcon Holdings Inc., chart prepared by AGNB

Advisory Board put in place too late

2.120 Eventually, unless it can drastically restructure its operations to generate significant cash, a company in a debt spiral runs out of available credit and goes bankrupt. This is

²⁵ Subordinated debt refers to a loan that ranks after other debts if a company falls into bankruptcy.

what happened to Atcon in the summer of 2009. As part of the conditions for its \$50 million in loan guarantees from the Province, Atcon was undertaking to sell or monetize its highway maintenance contract and its Swedish assets. It was also required to establish an Advisory Board acceptable to the Minister, and any contracts in excess of \$5 million were to be reviewed by the Advisory Board to ensure the anticipated profit margin, and the availability of working capital to undertake the contract, were acceptable. Unfortunately, Atcon was unable to monetize its assets and declared bankruptcy in 2010. We believe the Advisory Board was put in place too late to have a positive effect for Atcon.

Overall conclusion:
\$50 million new debt was not going to save Atcon

2.121 Atcon's financial downfall began in 2007, when it had inadequate working capital to support new volumes of business. Instead of self-funding operations, the company relied on debt and over the next three years exhausted the cash it could get from credit. A lack of cash forced Atcon to borrow money, meaning it was borrowing against future years' earnings. Though Atcon managed to increase its revenues in the years after 2007, the profit margin on the increased revenues was much lower.

2.122 Though we also have the benefit of hindsight, our analysis indicates the additional \$50 million in debt taken on by Atcon in July 2009, guaranteed by the Province, was insufficient to save the company from its eventual failure. Atcon was experiencing significant cash flow issues when it received the \$50 million from the Bank of Nova Scotia, but it did not receive a \$50 million cash injection. The majority of the \$50 million was used to pay down a line of credit and existing high interest debt, as well as various fees, taxes, liens and judgments. It was left with just under \$10 million of actual new credit, an amount that was not sufficient to solve its lack of cash flow and address its current liabilities of close to \$100 million. This is echoed in a note to a November 17, 2009 meeting of Atcon staff and the Advisory Board. The note states the "PNB financing was not sufficient to solve the problem" and "contracts are not self-funding – poor negotiated contracts."

Review carried out at the request of the Province identifies serious issues

2.123 The Province hired RSM Richter Inc., a firm of professionals, to review and comment on Atcon’s financial position at January 31, 2009 and its operating results for the year then ended. Their report, dated November 30, 2012 states Atcon had “serious accounting and financial reporting problems”²⁶ for at least two years before the Province provided Atcon with a \$50 million loan guarantee.

2.124 The report goes on to state there “appears to have been a systematic approach by management to overstate assets, revenues and profits, understate liabilities, expenses and losses.”²⁷ The firm estimated “Atcon’s assets and net earnings as at and for the year ended January 31, 2009, were overstated by an amount ranging from \$28.3 [million] to \$35.4 [million].”²⁸

Advisory Board made significant write-offs in 2009

2.125 As stated in the conditions for the \$50 million guarantee, Atcon was required to arrange an Advisory Board acceptable to the Minister. The first meeting of the Advisory Board was in September 2009. In Atcon Construction Inc.’s internal financial statements at October 31, 2009 (Atcon’s primary operating arm), certain significant adjustments were made that affected the income statement. The adjustments, totaling \$28.5 million, pertained mainly to work in progress, as well as insurance claims and deferred costs. Exhibit 2.23 provides a summary of the adjustments.

Exhibit 2.23 - Significant reductions to Atcon Construction Inc.’s income in October 2009

Significant reductions to Atcon Construction Inc.’s income in October 2009	
Work-in-progress	\$ 24,775,515
Insurance claim	887,550
Deferred costs	2,825,000
Reduction to income	\$ 28,488,065

Source: Financial records of Atcon Construction Inc., chart prepared by AGNB

²⁶ “Atcon overstated revenue by \$35.4M before loan guarantees”, by Daniel McHardie, CBC News, posted December 13, 2012.

²⁷ Ibid

²⁸ Ibid

2.126 In a presentation to the Advisory Board in November 2009, adjustments (reductions) to equity were estimated at \$32 million for Atcon Holdings (which includes the amounts shown in Exhibit 2.23).

2.127 The Richter report and the adjustments proposed by the Advisory Board address a number of similar issues. A summary of estimated adjustments identified by Richter, the Advisory Board and our office are shown in Exhibit 2.24.

Exhibit 2.24 - Summary of estimated adjustments to Atcon Holdings financial information

Summary of estimated adjustments to Atcon Holdings financial information			
Adjustment	Richter report estimated misstatements to Jan 31, 2009 financial statements ⁽¹⁾ (in millions)	Advisory Board write downs ⁽²⁾ (in millions)	AGNB irregularities noted in the January 31, 2009 financial statements (in millions)
Impairment of long-lived assets	\$10 to \$17	\$7.0	
Incorrect deferral of equipment lease payments	8.6	6.2	
Work-in-progress overstatement	15.6	19.7	
Deferred labour costs	2.5	2.5	
Claims allowance	1.0 - 3.5	2.0	
Other items		3.8	
Tax recoveries	(9.4) – (11.8)	(9.1)	
Financial statement reclassification			\$ 21.7
Total	\$ 28.3 - \$ 35.4	\$ 32.1	\$ 21.7

Source: ⁽¹⁾ “Atcon overstated revenue by \$35.4M before loan guarantees”, by Daniel McHardie, CBC News, posted December 13, 2012, and ⁽²⁾ Information package: Atcon Holdings external Advisory Board meeting November 17, 2009. Table created by AGNB

2.128 We note that Grant Thornton, in its statement of defense in the case of the Province of New Brunswick vs. Grant Thornton LLP, states “*the 2009 Financial statements present fairly Atcon’s overall financial position, results of operations and cash flows as at and for the fiscal year ended January 31, 2009*” and that they “*conducted an audit and prepared the 2009 Auditor’s Report in accordance with GAAS.*” The statement of defense also includes detailed explanations by Grant Thornton denying all estimated misstatements by Richter.

2.129 As a matter of professional courtesy, we provided Grant

Thornton the opportunity to read sections of an advance version of this report. Grant Thornton through its legal counsel provided the following response:

“Thank you for allowing the undersigned and Grant Thornton the opportunity to review draft excerpts from your report at your office on August 28, 2017.

Since we were not provided with a complete version of your report, it is difficult to comment on the excerpts provided without having the full and proper context. However, we would note that the amount management fully disclosed and reclassified from current liabilities to long-term liabilities in the January 31, 2009 consolidated balance sheet of Atcon Holdings Inc. (“Atcon”) was based on documents existing at that date related to Atcon’s credit facility agreement amendments and the relevant professional accounting standards and guidance at that time.

As you noted in the excerpts of your draft report provided for our review, there is currently an ongoing litigation matter and therefore we are unfortunately unable to comment further related to the above or additional matters.”

Ongoing Matters

Province slow in pursuing personal guarantee by Robert Tozer

2.130 The conditions for Atcon’s \$50 million guarantee included a personal guarantee from Robert Tozer, the President of Atcon Holdings Inc. This guarantee did not include Mr. Tozer’s personal residence.

2.131 We inquired with Opportunities NB as to the past use of personal guarantees as a means of security for financial assistance granted by the agency. We requested information on the use of personal guarantees for the past ten years (2006 to 2016) and the outcome when a guarantee is called.

2.132 The information provided by Opportunities NB indicates that there were six instances in the last ten years where personal guarantees were used, totalling over \$78 million. Of the six, three are on active loans while three have defaulted. The three defaulted loans had personal guarantees valued at \$53.4 million; to date, \$15,000 has been recovered on one guarantee while the other two guarantees are still in the courts.

We noted the length of time between the default and the date the Province calls on the personal guarantee can vary significantly, from ten months to five years. The personal guarantee on Robert Tozer is the one that took Opportunities NB five years to pursue.

2.133 During our 2015 audit of financial assistance provided to Atcon, we inquired of the Office of the Attorney General why government had not (at the time of our inquiry in December 2014) pursued the personal guarantee against Robert Tozer as a recovery on the defaulted guarantee. In their response, the Office of the Attorney General stated the personal guarantee was still in the name of the Bank of Nova Scotia, and once the Province received the title, it would be in a position to begin pursuing the guarantee.

2.134 Following the release of our 2015 Report *Financial Assistance to Atcon Holdings Inc. and Industry* in March 2015, the Province filed a Notice of Action with Statement of Claim attached against Mr. Tozer on May 19, 2015 for the personal guarantee. Mr. Tozer filed a statement of defense with the courts on July 20, 2015. We have been advised by the Office of the Attorney General that, as of July 2017, the matter:

“continues to be in the Document Discovery phase and no date has been set for an Examination for Discovery. It is unlikely that would begin before mid-2018.”

Province’s legal action against auditor of Atcon in process

2.135 In June 2014, the Province commenced legal action against the auditor of Atcon Holdings Inc. Statements of claim and defence have been filed. The Province claims the auditor of Atcon, Grant Thornton, was negligent and in breach of its duties to the Province in conducting the external review of Atcon’s assets which was a precondition to the issuance of the guarantees, and in its audit of Atcon and rendering an unqualified audit opinion with respect to the fiscal 2009 financial statements. Grant Thornton has vigorously denied these claims. We have been advised by the Office of the Attorney General that, as at July 2017:

“the Plaintiff’s document identification, collection and review process for priority government paper documents is complete and near completion for government electronic information. Review of indexes of paper documents in the possession of the bankruptcy trustee has commenced. Examination of selected documents in the possession of the trustee will follow. No party has delivered an Affidavit of Documents yet. It is expected

that document disclosures, starting with paper documents, will commence by late 2017”

CPA professional conduct complaint not resolved

2.136 A professional conduct complaint was made by the Province of New Brunswick to the New Brunswick Institute of Chartered Accountants (now known as Chartered Professional Accountants (CPA) of New Brunswick) in the Atcon matter. In November 2016, we were advised by the President and CEO of CPA New Brunswick that:

“CPA New Brunswick’s statutory professional discipline body, the Complaints Enquiry Committee, concluded its preliminary investigation into the complaints of the Province of New Brunswick and have referred the matters for hearing by the organization’s Discipline Tribunal.”

2.137 The organization is working towards the logistics of scheduling a hearing on the matter, and the hearing process is expected to start during the fall of 2017.

Cabinet Ministers at the time knew the risks

2.138 We met individually with each of six Cabinet Ministers who were part of the decision to provide the \$50 million in loan guarantees to Atcon in July 2009, as well as the September 2009 decision to release the Province’s security in favour of the Bank of Nova Scotia. It is positive to note all six Cabinet Ministers were cooperative and forthcoming in agreeing to be interviewed.

2.139 We learned the process for reviewing requests for assistance now is different than the process in place in 2009. The Cabinet Ministers described the current process as more robust. The Ministers also affirmed that at the time of the decision in 2009, they claimed to have understood the risks involved with the request from Atcon, and spent significant time discussing the file. As noted in our 2015 Atcon report, even though senior officials repeatedly advised against it, Cabinet approved the \$50 million in guarantees.

2.140 The six Cabinet Ministers provided a consistent rationale for granting financial assistance to Atcon. Based on our interviews, it appears the decision to grant financial assistance to Atcon, despite the significant risks involved, was due to a number of factors including:

- Already depressed economy in the Miramichi region;
- Large number of businesses across New Brunswick that

would be negatively affected should Atcon fail; and

- Atcon’s plans moving forward looked promising.

2.141 In our 2015 report, we stated “*no rationale was documented or evident for the decision to approve the request to release the first security interest, despite the risks identified by staff. We do not understand why Cabinet approved this request as it appeared to have transferred the impact of the pending loss from the bank to the taxpayer.*”²⁹ During our interviews with the six Cabinet Ministers, no clear rationale was provided for the decision to release security on the guarantees in favour of the Bank of Nova Scotia.

Cabinet released security as Advisory Board gets underway

2.142 Based on our interviews, it appears a lot of hope was placed solely on the fact that well-known business leader with a “convincing record of being able to help troubled companies”³⁰, was going to head the Advisory Board of Atcon. On September 10, 2009 a letter from then Minister of Business New Brunswick was sent to this individual, thanking him for agreeing to be part of the Advisory Board of Atcon. The following day, on September 11, 2009, Cabinet authorized the Minister of Business New Brunswick to release the security held by the Province in favour of the Bank of Nova Scotia.

Cabinet Ministers interviewed offered no clear answers for the release of security

2.143 We consider the decision to release the security as the critical failure in the Atcon file, resulting in significant losses for taxpayers. The security held by the Province was an important mitigating factor against the significant risks posed by this file, yet the Cabinet Ministers we spoke to could offer no clear explanation for their decision.

Follow up 2015 Atcon recommendations

2.144 We have received updates from the Executive Council Office (ECO) and ONB on the status of the recommendations made in our 2015 audit *Financial Assistance to Atcon Holdings Inc. and Industry*. Both the ECO and ONB report they have acted quickly to respond to our recommendations. In their

²⁹ 2015 Report of the Auditor General, Volume 1, *Financial Assistance to Atcon Holdings Inc. and Industry*, par. 2.55

³⁰ Paragraph 124 (p.40) of *Report to the Speaker of the Legislative Assembly of New Brunswick of the Investigation/Inquiry by the Hon. Patrick A.A. Ryan, Q.C. Conflict of Interest Commissioner into Allegations by Mr. Claude Williams, MLA for Kent South of Violations of the Members’ Conflict of Interest Act by Premier Shawn Michael Graham, MLA for Kent*

updates, they indicated they had implemented 15 of our 19 recommendations by the end of 2016.

2.145 In January 2017, we reviewed the assertions made by ONB for accuracy by examining new or improved initiatives implemented by ONB, and checking for supporting evidence to verify that implementation has, in fact, occurred. We also tested a sample of loan files. We returned again in July 2017, testing additional files. Exhibit 2.25 shows the recommendations, the responses from ONB and ECO and our assessed status.

So far ONB and ECO have implemented 4 of 19 recommendations

2.146 In the update provided by ONB, it assessed 15 of the 19 recommendations as implemented and the remaining four recommendations as “in-progress”. During our review, we determined ONB and ECO have implemented 4 of our 19 recommendations. For the remaining 11 recommendations that ONB reported as implemented, it is positive to note that ONB made progress in the development of policies and guidelines, but during testing we found exceptions in its application, resulting in a finding of “not implemented” for these recommendations. Although there has been progress by ONB, for recommendation 2.98 in Exhibit 2.25 involving the Executive Council Office, we found little effort by ECO to ensure our recommendations have been applied to all other entities providing financial assistance to industry, as evidenced in their response to the recommendation.

Little effort by ECO to ensure recommendations are applied to all entities providing financial assistance to industry

Taxpayer unable to assess past performance of financial assistance to industry

2.147 It does not appear that ONB intends to implement one of our recommendations. For recommendation 2.123 in Exhibit 2.25, concerning the need to track and report the actual performance of the past ten years of financial assistance to industry, ONB has indicated that “while tracking the historical performance of financial assistance is an important exercise and that it is prudent to continue this practice into the future, we do not believe the benefit of a 10 year look back will justify the substantial cost and investment.”³¹ We are disappointed with the response to this recommendation. By only assessing performance on a go-forward basis, there will be no accountability on past actual performance of financial assistance to industry, and we will never be able to determine if

³¹ CFO Report “Response to Auditor General Recommendations” October 15, 2016, p.69

the outcome of financial assistance to industry is an effective use of taxpayers' money.

Exhibit 2.25 - Status of recommendations made as a result of 2015 audit Financial Assistance to Atcon Holdings Inc. and Industry

<p>Recommendation: 2.38 We recommend the Department establish clear guidelines for applications for assistance with documented analysis maintained in the client file to ensure decisions are supported.</p>	
<p>Departmental response:</p> <p>Implemented</p> <p>ONB has developed policies and procedures for each type of assistance available to clients. This includes standard forms where specified analysis and information is required for application approval.</p> <p>Depending on the type of assistance, standard models have been developed to analyze payroll rebates, payroll support, forgivable loans, credit guarantees and repayable loans.</p>	<p>2017 status as assessed by AGNB:</p> <p>Implemented</p>
<p>Recommendation: 2.39: We recommend the Department ensure all requests for assistance include an application properly prepared and signed as complete and accurate by the client.</p>	
<p>Departmental response:</p> <p>Implemented</p> <p>As required under the ONB Act, Section 22(1) and the ONB Regulations, Sections 2(2) and 3, ONB has developed a "Request for Assistance" letter to be signed by the client covering these requirements and recommended additional inclusions by the Auditor General.</p>	<p>2017 status as assessed by AGNB:</p> <p>Not implemented</p> <p>We reviewed the template letter and tested a sample of files to assess its application. Based on our review, we found ONB did prepare a template letter with necessary components to satisfy our recommendation. However, we found exceptions to the use of the letter. In some instances, some components of the letter were missing or the letter was not used. As a result, we assessed the recommendation as not implemented.</p>

Exhibit 2.25- Status of recommendations made as a result of 2015 audit Financial Assistance to Atcon Holdings Inc. and Industry (continued)

<p>Recommendation: 2.41: We recommend the Department establish minimum standards and criteria, such as number of jobs to be created or maintained per dollar advanced, for use in evaluating applications for assistance.</p>	
<p>Departmental response:</p> <p>Implemented</p> <p>Under the guidance of the ONB Board of Directors, corporate targets have been set in ONB's first ever strategic plan. These corporate targets have been operationalized and the policies, procedures, standard forms, payroll model and credit model establish KPI's by type of assistance when evaluating assistance applications.</p>	<p>2017 status as assessed by AGNB:</p> <p>Not implemented</p> <p>We reviewed the various forms and models used in evaluating a request for assistance. Based on our review, we found ONB did establish targets for use in evaluating applications for assistance. However, for some of the files we sampled, the models described by ONB were not used. We will conduct further follow-up in the future to determine consistent use of the models. As a result, we assessed the recommendation as not implemented.</p>
<p>Recommendation: 2.45: We recommend the Department include a complete version of the most recent audited financial statements with Memorandums to Executive Council (MEC) requesting financial assistance.</p>	
<p>Departmental response:</p> <p>Implemented</p> <p>While the previous Department had been following this practice for several years, ONB has included this as a specific requirement in the ONB standard MEC.</p> <p>However, requests for assistance under specified levels may not require external nor internal statements if the risk exposure so warrants per procedures in place.</p>	<p>2017 status as assessed by AGNB:</p> <p>Not implemented</p> <p>We reviewed ONB's policy with regards to financial statements in ONB's matrix of documents required by level of assistance. We also found that the standard MEC does include a reminder to attach recent financial statements. However, during testing we found exceptions to the application. We found the required financial statements were not always included in the MECs. As a result, we assessed the recommendation as not implemented.</p>

Exhibit 2.25- Status of recommendations made as a result of 2015 audit Financial Assistance to Atcon Holdings Inc. and Industry (continued)

<p>Recommendation: 2.57: We recommend the financial considerations included in the Memorandum to Executive Council (MEC) clearly state the financial impact on the accounts of the Province, including the need for a provision for loss.</p>	
<p>Departmental response:</p> <p>Implemented</p> <p>While the previous Department had been following this practice for several years, ONB has included this as a specific requirement in the ONB standard MEC.</p>	<p>2017 status as assessed by AGNB:</p> <p>Not implemented</p> <p>We reviewed the standard MEC and found it does include the sections described by ONB. During testing, we found some of the files sampled, where a provision for loss was possible, did not always include a discussion of the need for provision for loss. As a result, we assessed the recommendation as not implemented.</p>
<p>Recommendation: 2.61: To improve future economic development decision making, we recommend the Department quantify the risks and rewards to the Province in order to clearly establish and balance the value received for the output of funding and the risk assumed by the Province.</p>	
<p>Departmental response:</p> <p>Implemented</p> <p>While the previous Department had been following this practice for several years, ONB has included this as a specific requirement in the ONB standard MEC.</p> <p>In addition, the payroll model and credit model provide additional risk analysis.</p>	<p>2017 status as assessed by AGNB:</p> <p>Not implemented</p> <p>We tested a sample of files against the assertions in ONB's response. We found ONB has tools to quantify and analyze the risks and rewards and the standard MEC does include sections to communicate the risks and rewards involved in a request for assistance. However, for some of the files we sampled, the models described by ONB were not used. We will conduct further follow-up in the future to determine consistent use of the models. As a result, we assessed the recommendation as not implemented.</p>

Exhibit 2.25- Status of recommendations made as a result of 2015 audit Financial Assistance to Atcon Holdings Inc. and Industry (continued)

<p>Recommendation: 2.64: <i>We recommend the Department establish guidelines for verification of claims and assumptions underlying projections included in applications for financial assistance.</i></p>	
<p>Departmental response:</p> <p>In-Progress</p> <p>The 2014 Reference Guide is in place, the ONB policies and procedures are updated and the final phase is a standard file system/check list for a company in general and specific to the type of assistance requested.</p>	<p>2017 status as assessed by AGNB:</p> <p>Not implemented</p> <p>Response indicates implementation is in progress; therefore we assessed the recommendation as not implemented</p>
<p>Recommendation: 2.65: <i>We recommend all claims of job creation or maintenance, in connection with the application, be made in writing, supported by documentation and signed by a company representative indicating the accuracy of the documentation and the company's commitment.</i></p>	
<p>Departmental response:</p> <p>Implemented</p> <p>This recommendation is incorporated in the "Request for Assistance" letter.</p>	<p>2017 status as assessed by AGNB:</p> <p>Not implemented</p> <p>Based on our review, we found ONB has developed a "request for assistance" letter template which addresses the intent of our recommendation. However, we found exceptions in the use/application of the letter in our sample of files tested. In some instances, some components of the letter were missing or the letter was not used. As a result, we assessed the recommendation as not implemented.</p>

Exhibit 2.25- Status of recommendations made as a result of 2015 audit Financial Assistance to Atcon Holdings Inc. and Industry (continued)

<p>Recommendation: <i>2.72: We recommend the Department, in collaboration with others, propose an update to the Economic Development Act and Regulation to clarify the authority to amend security.</i></p>	
<p>Departmental response:</p> <p>Implemented</p> <p>This recommendation has been addressed by Section 24 of the ONB Act. This Section specifies the requirements for security to which management adheres.</p>	<p>2017 status as assessed by AGNB:</p> <p>Implemented</p> <p>Per paragraph 24(1.1) of the ONB Act, the authority to release security rests with Opportunities NB; when the amount exceeds \$2 million, approval of the Lieutenant-Governor-in-Council is required. However, paragraph 24(1.2) states ONB may release security on any terms and conditions it specifies if it considers the release of security does not substantially impact the financial risk of the Province.</p> <p>As a result, we assessed the recommendation as implemented as the Act places the statutory authority to amend security with ONB, as represented by the Board.</p>
<p>Recommendation: <i>2.82: Where it would improve the security taken by the Province on loan agreements, we recommend the Department seek an independent assessment of assets when assets are provided as security on loan or guarantee agreements, especially where the value is significant. Should further financial assistance be requested, the Department should reassess the value of these assets as this may affect the realizable value of the security.</i></p>	
<p>Departmental response:</p> <p>Implemented</p> <p>ONB policy is to require confirmation of value for all assets secured over \$200,000 in value. Such confirmation includes appropriate professional valuations or third party invoices less than 12 months old.</p>	<p>2017 status as assessed by AGNB:</p> <p>Not implemented</p> <p>Based on our review of ONB Policy #06E on Repayable loans, we found ONB has established guidelines for obtaining support for the value of assets pledged as security. However, we found exceptions to the application of the policy. Of the files sampled where security was pledged, none had third party independent valuation of assets. As a result, we assessed the recommendation as not implemented.</p>

Exhibit 2.25- Status of recommendations made as a result of 2015 audit Financial Assistance to Atcon Holdings Inc. and Industry (continued)

Recommendation:	
2.83: <i>When personal guarantees are provided, we recommend the Province ensure there is adequate evidence to support the value of the personal assets such that there is sufficient net worth to safeguard taxpayers' money.</i>	
Departmental response:	2017 status as assessed by AGNB:
<p>Implemented</p> <p>ONB policy is to require confirmation of personal net worth for a personal guarantee. Such confirmation is acceptable in the form of a certified letter from a designated professional.</p>	<p>Not implemented</p> <p>Based on our review of ONB Policy #6E, ONB has established guidelines for confirmation of personal net worth for a personal guarantee, including a certified letter from a designated professional. During testing, we found such a letter as confirmation for a significant personal guarantee. However, a letter alone, with no additional information, is not sufficient to comply with our recommendation. Further information, such as detailed value by asset type obtained on an annual basis, would provide adequate evidence to support the value of assets pledged. As a result, we assessed the recommendation as not implemented.</p>

Exhibit 2.25- Status of recommendations made as a result of 2015 audit Financial Assistance to Atcon Holdings Inc. and Industry (continued)

<p>Recommendation: 2.85: <i>We recommend the Department clearly identify companies and individuals involved in past defaults on government financial assistance as part of the Memorandum to Executive Council (MEC). Where there is a recommendation to approve assistance to such a company or individual, the justification should be clearly stated on the MEC.</i></p>	
<p>Departmental response:</p> <p>Implemented</p> <p>While the previous Department had been following this practice for several years, ONB has included this as a specific requirement in the ONB standard MEC.</p> <p>ONB also requires justification for new/additional assistance in such cases.</p>	<p>2017 status as assessed by AGNB:</p> <p>Not implemented</p> <p>We reviewed the standard MEC and it does include the sections as described in the response. We also examined a sample of files for the use of the “Request for Financial Assistance” application form which requires companies to disclose all details of financial assistance from any government department or agency over the past five years. We found some instances where the form was not used and therefore did not provide the disclosure necessary to fulfill this requirement. As a result, we assessed the recommendation as not implemented.</p>

Exhibit 2.25- Status of recommendations made as a result of 2015 audit Financial Assistance to Atcon Holdings Inc. and Industry (continued)

<p>Recommendation: 2.95: We recommend the Department establish a limit on the amount of assistance/level of provincial exposure that can be granted to a single company or group of related companies.</p>	
<p>Departmental response:</p> <p>In Progress</p> <p>Management has prepared a policy on corporate, group and industry limits for the "active loan portfolio". This policy is being presented to the ONB Board for approval in May 2016.</p> <p><u>[AGNB note: this policy was subsequently approved by the ONB Board and became effective February 8, 2017]</u></p>	<p>2017 status as assessed by AGNB:</p> <p>Implemented</p> <p>Based on our review, ONB has established limits on financial assistance. Policy #08 establishes the limits of ONB’s loan portfolio exposure based on any of the following components:</p> <ul style="list-style-type: none"> • More than 30% of active portfolio; • More than 75% of debtor’s tangible net worth; • Debtor’s net equity is less than 20% post project/financing; and • Industry exposure is > 50% of active portfolio. <p>The policy states “ONB shall <i>not normally</i> look to increase its exposure.” This indicates to us that there is no absolute limit on the amount of assistance or level of provision exposure that can be granted to a single company or group of related companies.</p>
<p>Recommendation: 2.96: We recommend the Department implement a process whereby financial assistance to industry provided by all government departments/agencies is monitored to determine the extent of financial assistance granted by all agents in the government reporting entity.</p>	
<p>Departmental response:</p> <p>Implemented</p> <p>While the previous Department had been following this practice for several years, ONB has included this as a specific requirement in the ONB standard MEC.</p> <p>In addition, the new "Request for Assistance" letter requires applicants to disclose such past assistance and ONB also requires a "Letter of Support" for an applicant from sister departments (forestry, fisheries, etc.) when the applicant operates in a specified sector.</p>	<p>2017 status as assessed by AGNB:</p> <p>Not implemented</p> <p>We reviewed the standard MEC and it does include the sections as described in the response. We also examined a sample of files for the use of the “Request for Financial Assistance” letter and found some instances where the letters were either not used or responses did not include disclosure re details of financial assistance from other departments or agencies. As a result, we assessed the recommendation as not implemented.</p>

Exhibit 2.25- Status of recommendations made as a result of 2015 audit Financial Assistance to Atcon Holdings Inc. and Industry (continued)

Recommendation: 2.97: We recommend, as an efficiency measure and to streamline administration, the Department of Economic Development make recommendations to Cabinet to rationalize the number of provincial entities that provide financial assistance to industry.	
Departmental response:	2017 status as assessed by AGNB:
<p>Implemented</p> <p>On April 1st, 2015, Invest NB and the Department of Economic Development were combined into Opportunities NB.</p> <p>In January 2016, ONB recommended the closure of certain provincially held corporations and the transfer of the associated loan portfolios to ONB.</p> <p>ONB will continue to work with Executive Council Office, Jobs Board and other departments to make such recommendations as the appropriate circumstances arise.</p>	<p>Not implemented</p> <p>Based on the response provided, we do not find the situation has changed in an impactful manner. As a result, we found the intent of our recommendation has not been met and the recommendation has not been implemented. At the time of our 2015 report, six provincial entities could provide financial assistance; now there are five, mainly due to the creation of ONB. The five provincial entities are:</p> <ul style="list-style-type: none"> • Opportunities NB; • Dept. of Agriculture, Aquaculture and Fisheries; • Dept. of Post-Secondary Education, Training and Labour; • Regional Development Corporation; and • Provincial Holdings.

Exhibit 2.25- Status of recommendations made as a result of 2015 audit Financial Assistance to Atcon Holdings Inc. and Industry (continued)

<p>Recommendation: 2.98: <i>We recommend the Executive Council Office take responsibility for coordinating the implementation by all departments/agencies providing financial assistance to industry of recommendations of this report.</i></p>	
<p>Response from Executive Council Office:</p> <p>The Executive Council Office has assumed responsibility for ensuring that the recommendations of the Auditor General are being addressed across all departments/agencies that have authority to provide financial assistance to industry. Currently, almost all financial assistance to industry is being provided through Opportunities New Brunswick (ONB). ONB has been very actively pursuing process changes to address the recommendations emanating from the Atcon file; these accomplishments have been submitted under separate cover.</p> <p>Response from ONB:</p> <p>In Progress</p> <p>Opportunities NB has committed to reviewing the feasibility of this recommendation with the Executive Council Office in fiscal 2016/2017 after completion and implementation of the recommendations directly under ONB control.</p>	<p>2017 status as assessed by AGNB:</p> <p>Not implemented</p> <p>Response indicates implementation is in progress; therefore we assessed the recommendation as not implemented.</p>

Exhibit 2.25- Status of recommendations made as a result of 2015 audit Financial Assistance to Atcon Holdings Inc. and Industry (continued)

Recommendation: 2.113: We recommend the Department report both expected and actual results of job creation and job maintenance in their annual report.	
Departmental response:	2017 status as assessed by AGNB:
<p>Implemented</p> <p>The ONB Board of Directors has directed these job statistics be published as a section of ONB's annual report.</p>	<p>Not implemented</p> <p>The intent of our recommendation is for ONB to report jobs <i>expected to be created</i> and the <i>jobs actually created</i>.</p> <p>To identify the targets, we reviewed ONB's 2016-2019 Strategic Plan. We found ONB has established annual targets for committed (expected) jobs and created (actual) jobs for the years 2015-16 to 2018-19. For example, the targets for the 2015-16 year were:</p> <ul style="list-style-type: none"> • Total jobs committed: 1,556 • Total jobs created: 829 <p>To identify the results reported, we reviewed ONB's 2015-2016 Annual Report. In it ONB asserts "<i>We surpassed our job creation target – committing a total of 2,965 jobs, nearly double our target of 1,500.</i>" ONB is speaking to "expected" jobs, not actual.</p> <p>Further, in the "Major Accomplishments" section of the annual report, ONB has reported "<i>2,965 jobs created. Nearly double our target of 1,500</i>". Once again, based on the figures, ONB is reporting on "expected" jobs, though has used the word created (implying actual).</p> <p>Our review of the annual report found that ONB has reported on the number of jobs expected to be created, but not on jobs actually created. We also found the inconsistent use of the terms "committed" and "created" made it difficult to assess the actual outcome achieved by ONB. As a result, we assessed the recommendation as not implemented.</p>

Exhibit 2.25- Status of recommendations made as a result of 2015 audit Financial Assistance to Atcon Holdings Inc. and Industry (continued)

<p>Recommendation: 2.123: We recommend the Department annually track and report the 10-year history of actual performance of assistance provided to industry, based on the 2010 analysis performed by the Office of the Comptroller.</p>	
<p>Departmental response:</p> <p>In Progress</p> <p>Opportunities NB has committed several staff to this project and hired an external audit firm to oversee and report on the findings.</p> <p>Phase 1 of the review includes three historical years (ED & INB) plus ONB's first year of operations. Subsequent to the Phase 1 report, management and the external audit firm will evaluate the feasibility of analyzing additional years based on cost, time, effort, information availability etc.</p>	<p>2017 status as assessed by AGNB:</p> <p>Not implemented</p> <p>Response indicates implementation is in progress; therefore we assessed the recommendation as not implemented. However, in a report to the Board Chair and CEO of ONB in October 2016, the CFO indicates ONB doesn't intend to implement this recommendation, stating "while we believe this is an important exercise and that it is prudent to continue this practice in the future, we do not believe the benefit of a 10 year look back will justify the substantial cost and investment."</p>
<p>Recommendation: 2.127: We recommend the Department establish goals, objectives and measurable targets for its financial assistance to industry programs.</p>	
<p>Departmental response:</p> <p>Implemented</p> <p>Under the guidance of the ONB Board of Directors, corporate targets have been set in ONB's first ever strategic plan. These corporate targets have been operationalized and the policies, procedures, standard forms, payroll model and credit model establish KPI's by type of assistance when evaluating assistance applications.</p>	<p>2017 status as assessed by AGNB:</p> <p>Implemented</p>

2.148 We will continue to follow-up and report on these recommendations in the future as part of our follow-up procedures.

Recommendations **2.149** An in-depth analysis of certain Atcon accounts, as we performed during this examination, could have provided significant insight to the depth of Atcon's financial difficulties and better information to decision makers. This analysis could also determine whether the amount of financial assistance requested is sufficient for the purpose requested, and if not, where the remaining financing will come from.

Conduct in-depth, multi-year analysis of financial condition

Recommendation **2.150** **Where the financial assistance requested is significant and is considered high risk, we recommend a clear determination be made and presented to Cabinet as to whether the amount of financial assistance requested is sufficient for the purpose intended.**

Include industry standards in analysis **2.151** A comparison of certain key ratios, as determined by ONB, to industry standards can serve as a tool to assess the financial condition of an entity requesting financial assistance.

Recommendation **2.152** **Where the financial assistance requested is significant and is considered high risk, we recommend information presented to Cabinet for decisions on financial assistance should include comparisons to industry standards to assess the health of the company requesting financial assistance.**

Amounts owed by shareholder and affiliated companies **2.153** When financial assistance was granted to Atcon Holdings Inc., records indicate the shareholder owed the company close to \$500,000 and an affiliated company owed approx. \$1.3 million to Atcon. In our opinion, where the amount of financial assistance is significant and there is high risk, financial assistance from the Province should not be provided to companies that are owed amounts from shareholders and affiliated companies.

Recommendation **2.154** **Where the financial assistance requested is significant and is considered high risk, we recommend no financial assistance be granted to a company when significant amounts are outstanding from the shareholders of the company or from affiliated companies. Any exceptions should be rare and well justified.**

Disclosures and representations by management and shareholders

2.155 We believe when significant financial assistance is being provided by the Province, the management and shareholders requesting the assistance should provide certain pertinent information as part of the application process. This would allow the Department to be well informed of the risk associated with a company, and the transfer of wealth within the company. If a company is transferring significant amounts to related parties prior to requesting financial assistance from the Province, this information could (and should) affect the decision to provide financial assistance. Such information could include:

- Salaries to key executives for the last three to five years;
- Salaries, dividends, bonuses to shareholders or family members for the last three to five years;
- Transfers to related/associated/affiliated companies in the last three to five years;
- Details of shareholder account activity (including loans) during the last three to five years; and
- Details of dividends, share redemptions and changes in share capital in the last three to five years.

Recommendation

2.156 **Where the financial assistance requested is significant and is considered high risk, we recommend management and shareholders be required to make a declaration pertaining to dividends, salaries, bonuses (or other) as needed as part of the application process; such as:**

- **Salaries to key executives for the past three to five years;**
- **Salaries, dividends and bonuses to shareholders and family members for the past three to five years;**
- **Transfers to related/associated/affiliated companies in the past three to five years;**
- **Details of shareholder account activity during the past three to five years; and**
- **Details of dividends, share redemptions and changes in share capital in the past three to five years.**

Restrictions on the payment of dividends

2.157 If a company is high risk and has received significant financial assistance from the Province, the payment of dividends, during the term of the financial assistance, should be

restricted.

Recommendation 2.158 Where the financial assistance requested is significant and is considered high risk, we recommend that agreements contain a restriction to require the approval of ONB prior to a dividend or bonus payment.

Significant declarations should be verified **2.159** As part of the conditions of its financial assistance, Atcon was required to pay all outstanding payables owed to New Brunswick companies. A declaration of such was provided by Atcon. Our examination could not determine whether these New Brunswick companies actually received payment as stated. We believe declarations as significant as this one should be verified in some manner to ensure the condition has been met.

Recommendation 2.160 Where the financial assistance requested is significant and is considered high risk, we recommend that statutory declarations made as a condition of financial assistance be verified.

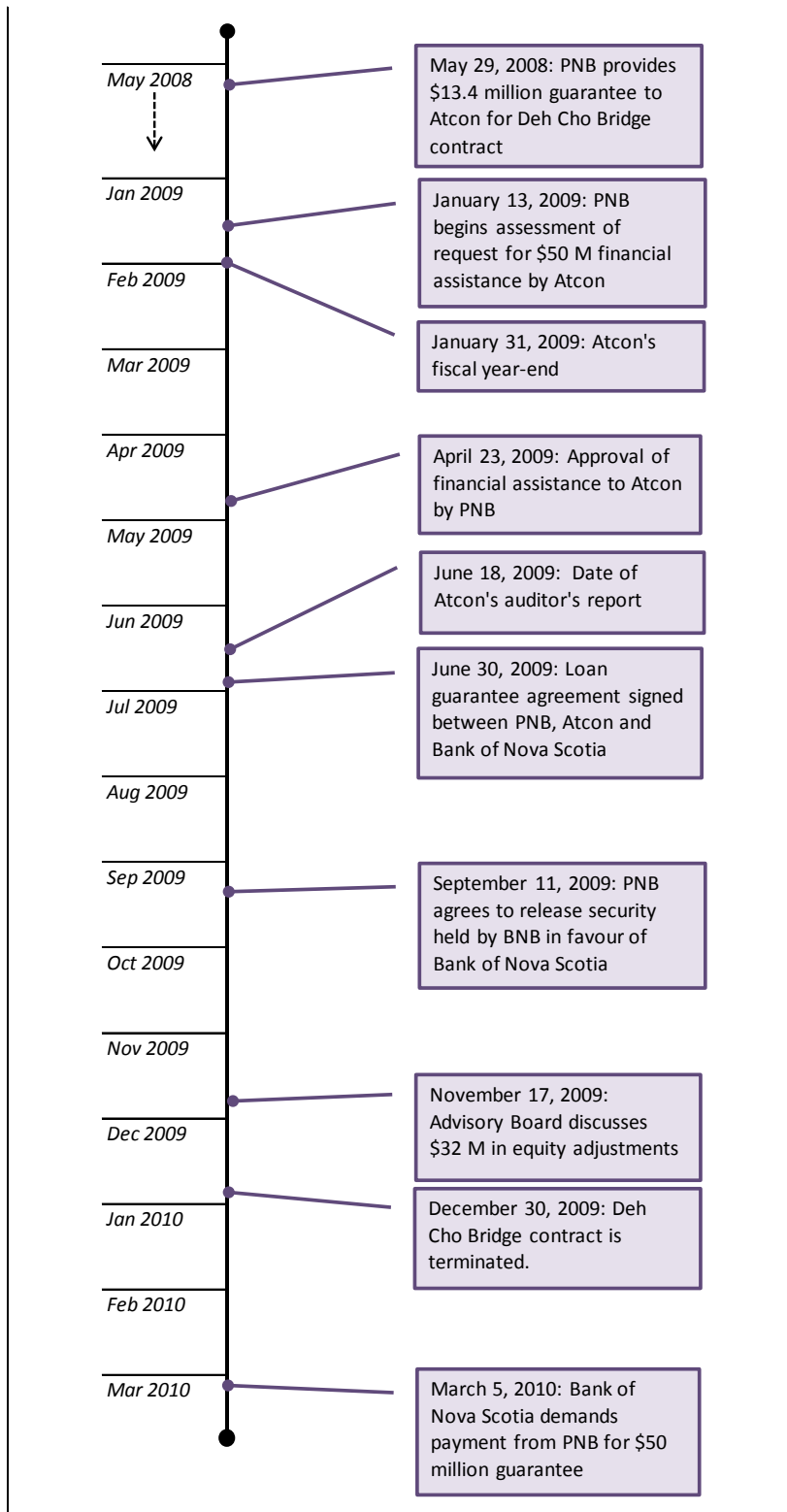
Personal guarantees should be pursued in a timely manner **2.161** The Province's security on the \$50 million guarantee included a personal guarantee from Robert Tozer. Though Atcon defaulted on its financial assistance in March 2010, the Province did not pursue the personal guarantee until May 2015. We believe personal guarantee should be pursued in a timely manner.

Recommendation 2.162 Where the Province has personal guarantees as security on financial assistance, we recommend ONB put in place a process whereby, in the event of default by the recipient, personal guarantees are promptly pursued.

2.163 Our recommendations are made in the hopes of improving the performance of financial assistance programs across government. Given there are five departments/agencies providing financial assistance to industry, we have recommended the Executive Council Office coordinate the implementation of our recommendations by all entities providing funding for economic development purposes.

Recommendation 2.164 We recommend the Executive Council Office take responsibility for coordinating the implementation of recommendations in this report by all departments and agencies providing financial assistance to industry.

Appendix I: Timeline of key events



Source: diagram prepared by AGNB based on information reported in 2015 audit *Financial Assistance to Atcon Holdings Inc. and Industry* and information found in Atcon files.