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REPORT TO FINANCE COMMITTEE MEETING OF WEDNESDAY, MAY 04, 2022

SUBJECT **CRD 2021 Audit Findings Report and Statement of Financial Information**

ISSUE SUMMARY

To approve the Capital Regional District (CRD) 2021 Statement of Financial Information (SOFI) and receive the 2021 Audit Findings Report for information.

BACKGROUND

The *Local Government Act* and the *Community Charter* require local governments to prepare financial statements each calendar year in accordance with Generally Accepted Accounting Principles and Canadian Public Sector Accounting Board (PSAB) standards. In addition, the statements must be independently qualified by an auditor.

The financial statements, along with the annual filing of the Local Government Data Entry (LGDE) form, must be submitted to the Inspector of Municipalities and available for public viewing by May 15. The Statement of Financial Information and the annual report must be completed by June 30 annually.

With the annual audit complete, and in alignment with PSAB regulations, management has prepared the required five statements with explanatory notes:

1. Statement of Financial Position
2. Statement of Operations
3. Statement of Change in Net Debt
4. Statement of Remeasurement Gains and Losses
5. Statement of Cash Flows

In addition, the 2021 Consolidated Statements of Financial Information (Appendix A) include:

1. Schedule of Remuneration and Expenses – Employees
2. Schedule of Remuneration and Expenses – Directors & Alternate Directors
3. Schedule of Remuneration and Expenses – Committee & Commission Members
4. Schedule of Remuneration and Expenses – Project Board Members
5. Statement of Severance Agreements
6. Schedule of Payments to Suppliers for Goods and Services
7. Schedule of Guarantee and Indemnity Agreements

To complete the financial package the following appendices are also included:

- B. Unaudited statements that present long term debt, reserve and financial statements for each service
- C. Analysis of the Statement of Change in Net Debt, Statement of Remeasurement Gains and Losses, and Statement of Cash Flows
- D. Canadian Municipal Governments Credit Rating Methodology used to measure the CRD

- E. Financial indicator analysis on the 2021 CRD results
- F. The 2021 Audit Findings Report from KPMG

The Audit Findings Report summarizes responsibilities of the auditor, scope of work, and audit results. The report also confirms there were no significant changes in the audit approach from the Audit Planning Report presented to the Board on January 5, 2022, and the audit findings confirm the financial statements present fairly, in all material respects, the financial position of CRD as at December 31, 2021.

ALTERNATIVES

Alternative 1

The Finance Committee recommends to the Capital Regional District Board:
That the Capital Regional District 2021 Statement of Financial Information be approved.

Alternative 2

That the Capital Regional District 2021 Statement of Financial Information be referred back to staff for additional information.

IMPLICATIONS

Financial Implications

Audit Findings Report

The Auditor's opinion is included as part of the Independent Auditors' Report within the financial statements (Appendix A).

The Audit Findings report (Appendix F) provides the results of their audit, and further discusses areas of focus identified in the Audit Planning Report presented to Board on January 5, 2022. Also included in the report is a summary of uncorrected adjustments on pages 11 and 22. Adjustments made during the course of audit field work are a result of both findings by management and KPMG through various reconciliation and testing activities.

Adjustments may remain uncorrected when an element of uncertainty exists and/or the adjustment has a material impact on accounting activities in a defined period but not considered to have an impact on decision making. All uncorrected adjustments are below the materiality threshold determined by the auditor. KPMG concurs with management's assessment of year-end adjustments.

Financial Statements

The Consolidated Statement of Financial Position and the Consolidated Statement of Operations form the basis of the audited financial statements and are similar to the Balance Sheet and Income Statement in private organizations.

The Capital Region Housing Corporation (CRHC) financials are consolidated in the CRD financial statements, as required by PSAB Standards.

HIGHLIGHTS

1. Consolidated Statement of Financial Position

The Statement of Financial Position highlights the following four key elements that together describe the financial status of the organization:

- a. Financial Assets and Liabilities (cash resources and obligations)
- b. Net Debt position (calculated as the difference between financial assets and liabilities)
- c. Non-financial assets that are held for service provision (such as tangible capital assets), and
- d. The accumulated surplus (referred to as equity in private organizations).

Financial Assets

Financial assets are non-physical assets whose value is derived from a contractual claim. The financial assets as of year-end consist of cash, investments, accounts receivable and debt recoverable from member municipalities. Total financial assets were \$603.0 million as of year-end, an increase of \$54.5 million or 10% from prior year. Table 1 summarizes financial assets as of December 31 with comparative changes year over year:

Table 1 – Change in Financial Assets Year over Year (\$ millions)

Description	2021	2020	\$ Change	% Change
Cash and Cash Equivalents	144.1	176.9	(32.8)	(19%)
Investments	213.5	185.7	27.8	15%
Accounts Receivable	55.8	35.0	20.8	59%
Member & Third Party Debt	185.5	146.9	38.7	26%
MFA Debt Reserve Fund	4.1	4.0	0.1	2%
Total Assets	\$603.0	\$548.5	\$54.5	10%

Cash and cash equivalents include cash on hand, bank deposits and cashable investments. The balance decreased in 2021 by (\$32.8) million (\$176.9 million to \$144.1 million). Further detail on changes in cash are discussed in Appendix C: Other Financial Statement Analysis, under Consolidated Statement of Cash Flows.

Investments include short (\$149.9 million) and long term holdings (\$63.6 million). Investments increased compared to 2020 by \$27.8 million consistent with savings targets set within each service. The year-end investment balance will vary depending on timing of operational cash needs.

Accounts receivables are due through the normal course of business. The balance at year-end will vary as a result of the timing of invoicing and payments. The increase of \$20.8 million, or 59% from prior year, was due to a federal grant receivable outstanding at year-end of \$36.2 million relating to the Residuals Treatment Facility offset by a prior year Wastewater Treatment Plant (WTP) federal grant receivable of \$17.0M that was collected during the year.

In the financial statements, debt recoverable from member municipalities and other third parties represents the amounts due from other organizations for their MFA financing obligations. New for 2021 is debt obligations from the Vancouver Island Regional Library (VIRL) related to a new

building. As the CRD flows payments through to the MFA, a liability equal to the receivable is also recorded, resulting in no impact on CRD's net debt position. Of the total \$185.5 million due, \$179.5 million from member municipalities and \$6 million from the VIRL. Member municipality debt increased by \$32.7 million or 22%, consisting of \$45.4 million in additional borrowing offset by (\$12.7) million of repayments, resulting in a year-end balance of \$179.5 million.

The debt reserve fund is the amount held by the MFA as security for debt obligations issued to the District. These amounts are refundable, with interest upon debenture maturity. Cash deposits of \$4.1 million (excluding member municipalities) are presented as a receivable on the financial statements. This balance changes in alignment with debt issues and maturities.

Liabilities

Liabilities are obligations or debt that will be settled through financial assets. These obligations represent the costs for goods and services consumed and owed by the CRD. Liabilities are used to finance operations and capital construction or acquisitions. As of December 31, 2021, liabilities totaled \$702.0 million, an increase of \$73.2 million or 12% from prior year. Table 2 provides balances and year over year changes:

Table 2 – Change in Liabilities Year over Year (\$ millions)

Description	2021	2020	\$ Change	% Change
Accounts Payable and Other Liabilities	31.0	117.1	(86.1)	(74%)
Deferred Revenue	49.0	32.7	16.3	50%
Short-Term Debt	25.7	61.3	(35.6)	(58%)
Long-Term Debt	582.9	405.0	177.9	44%
Landfill Closure and Post-Closure Liability	11.9	11.3	0.6	5%
Other Liabilities	1.5	1.5	0.0	0%
Total Liabilities	\$702.0	\$628.9	\$73.1	12%

Accounts payable decreased by (\$86.1) million or (74%) compared to 2020. The completion of the WTP resulted in a decrease in invoices payable of (\$14.2) million and release of construction holdback payables of (\$67.1) million.

The increase in deferred revenue of \$16.3 million or 50% is due to an increase of \$3.6 million in development cost charges in the Juan de Fuca Water Distribution service and an increase of \$12.1 million received through the Reaching Home and Rapid Housing grant program for housing projects that were unspent at year end.

Short-term debt details are disclosed in Note 3 to the financial statements. The balance decreased by \$35.6 million primarily due to \$61.3 million in short term debt converted into mortgages by CRHC for the Spencer and West Park properties. This is offset by new short-term borrowing of \$14.5 million for WTP, \$6 million in municipal debt for VIRL, and \$3 million for various electoral area capital projects.

Long-term debt includes balances for CRD, CRHC, and member municipalities where details are disclosed in Note 4 of the financial statements. Of the \$582.9 million in long-term debt, the CRD and CRHC portion is \$403.4 million, an increase of \$145.2 million or 56%. The increase is primarily driven by \$62 million for the capital financing portion of the Public Private Partnership

(P3) agreement for the Residuals Treatment Facility and by \$85.4 million for new mortgages for the Spencer, West Park and Hockley House affordable housing projects. The remaining portion of the \$582.9 million total long-term debt is \$179.5 million owed on behalf of member municipalities, which increased by \$32.7 million or 22%.

Landfill closure and post-closure liability increased by \$0.6 million, representing an additional year of capacity usage. This change year over year is not considered significant and aligns with expectations.

Non-Financial Assets

Non-financial assets are resources held for service delivery over one or more future periods. Examples include tangible capital assets, inventories of supplies, and prepaid portions of land leases. Table 3 lists balances of non-financial assets and changes from the previous year:

Table 3 – Change in Non-Financial Assets Year over Year (\$ millions)

Description	2021	2020	\$ Change	% Change
Tangible Capital Assets	1,949.4	1,760.5	188.9	11%
Other Non-Financial Assets	3.4	2.6	0.8	31%
Total Non-Financial Assets	\$1,952.8	\$1,763.1	\$189.7	11%

Non-financial assets increased by \$189.7 million to \$1.95 billion in 2021. This was mainly driven by an increase in tangible capital assets of \$188.9 million where acquisition or contributions were valued at \$248.1 million offset by \$58.5 million in amortization.

Significant asset acquisition or contributions include:

- \$166.7 million for WTP including the Residuals Treatment Facility
- \$30.6 million for the Hockley House property acquisition
- \$50.8 million in other capital projects including such as the Spencer Road housing project and Regional Parks land acquisitions.

Accumulated Surplus

The accumulated surplus or net book value of equity for the CRD is \$1.85 billion, where the organization has assets (Financial and Non-Financial) of greater value than what it owes (Liabilities). Table 4 summarizes accumulated surplus by category.

Table 4 – Accumulated Surplus Categories (\$ millions)

Description	2021	2020
Equity Invested in Tangible Capital Assets	1,526.4	1,441.1
Capital and Operating Reserves	170.3	141.4
Net Operating Funds	158.2	99.7
2021 Accumulated Surplus	\$1,854.9	\$1,682.2

2021 CRD net operating funds of \$158.2 million represents 8.5% of accumulated surplus. The remaining 91.5% of accumulated surplus resides in tangible capital assets (\$1,526.4 million) and capital and operating reserves (\$170.3 million).

Operating Reserve Funds enable each service area to set aside funds to mitigate fluctuations in revenue driven by cyclical expenditures, unforeseen expenses and special one-time operating projects. Capital Reserve Funds accumulate resources for future capital expenditures. Periodically, services transfer either budgeted or operating surplus funds to their respective capital reserve. The practice of building reserves for funding ongoing infrastructure renewal is essential to ensure long-term sustainability of asset-dependent CRD services.

2. Consolidated Statement of Operations

The Statement of Operations identifies results of financial activities for the fiscal year by presenting revenues less expenses on an accrual basis. Under accrual accounting and the matching principle, the CRD records economic events regardless of when cash is actually received or used, with the objective of matching period revenues with incurred costs.

As required by PSAB reporting standards, the budget authorized by bylaw is included on the Statement of Operations and has been adjusted to exclude reserve transfers and principal repayment to better align budget to actual revenue and expense.

Other differences from budget, that are not adjusted, remain where amounts are recorded for alignment to public sector accounting standards due to adjustments to actuals for elimination and classification purposes. These differences include labour allocations, inter-service recoveries, grant revenue, deferred revenue, donations and amortization expense.

Revenue

2021 Revenue was \$407.4 million, a decrease of (\$25.8) million or (6%). Revenue totals by type and changes from the previous year are summarized in Table 5:

Table 5 – Change in Revenue Year over Year (\$ millions)

Description	2021	2020	\$ Change	% Change
Government Transfers	258.4	302.1	(43.7)	(14%)
Sale of Services	87.8	77.7	10.1	13%
Other Revenue	21.6	16.3	5.3	33%
Interest Earnings	4.5	5.6	(1.1)	(20%)
Developer Contributions	4.1	5.7	(1.6)	(28%)
Affordable Housing – Rental Income	21.8	17.0	4.8	28%
Grants in Lieu of Taxes	3.6	3.6	0.0	0%
Actuarial Adjustment of Long-Term Debt	5.6	5.2	0.4	8%
Total Revenue	\$407.4	\$433.2	\$(25.8)	(6%)

Primary drivers for changes in revenue are:

- (\$43.7) million decrease in government transfers due to a (\$62.0) million decrease in provincial grants relating to the WTP, offset by a \$15.0 million increase in other provincial grants and a \$3.3 million increase in federal grants.

- \$10.1 million increase in sale of services due to \$6.1 million increase in water revenue and a \$3.2 million increase in Hartland landfill revenue.
- \$5.3 million increase in other revenues driven by an increase in land donations of \$2.0 million for 2782 Spencer Rd, \$2.3 million donation for 4692 Mountain Rd, and \$0.3 million for the Sun River Reservoir.
- (\$1.1) million decrease in interest earnings due to a decline in interest rates.
- (\$1.6) million decrease in developer contributions relating to water infrastructure assets and household water connections in the Juan de Fuca Water Distribution service.
- \$4.8 million increase in affordable housing revenue driven by rental units increasing from 1,773 to 1,893 in 2021, and a full year of rent for Spencer and West Park projects completed in 2020.
- \$0.4 million increase in actuarial adjustment of long-term debt. The actuarial adjustment of long-term debt is the estimated return on the invested balance of MFA principal repayments.

Expenses

Expenses in 2021 increased by \$51.8 million or 28% to \$234.6 million. As shown in the segmented reporting, note 19 in the financial statements, the change by expense type over the previous year is summarized in Table 6:

Table 6 – Change in Expenses Year over Year (\$ millions)

Description	2021	2020	\$ Change	% Change
Salaries, Wages and Benefits	74.5	68.9	5.6	8%
Contract for Services and Consultants	25.8	22.1	3.7	17%
Amortization of Tangible Capital Assets	58.5	33.8	24.7	73%
Interest on Debt	21.7	17.1	4.6	27%
Other Expenses	54.1	40.9	13.2	32%
Total Expenses	\$234.6	\$182.8	\$51.8	28%

Expense changes were driven by:

- \$5.6 million increase in salaries, wages and benefits relating to contractual agreements and increased staff resources.
- \$3.7 million increase in contract for services and consultants due to \$3.2 million of new costs for operations of the Residuals Treatments Facility.
- \$24.7 million increase in amortization on tangible capital assets due to WTP assets going into use and full year of amortization for the West Park, Spencer and Hockley House projects.
- \$4.6 million increase in interest due the completion of the Residuals Treatment Facility and mortgages for the Spencer, West Park and Hockley House properties.
- Other expenses increased by \$13.2 million driven largely by other expenses for WTP now in full operation. This resulted in a \$2.8M increase in supplies expense, \$2.2M increase in utilities expenses, and \$7.8M increase in costs allocations.

2021 Annual Surplus

The net difference between revenues and expenses for 2021 is an annual surplus of \$172.7 million. Summarized in Table 7 below are the change in accumulated surplus as a result.

Table 7 – Surplus Reconciliation (\$ millions)

Description	2021	2020
Increase in Capital Equity	85.3	197.6
Increase in Capital and Operating Reserves	28.9	3.6
Increase in Operating Funds	58.5	49.2
2021 Annual Surplus	\$172.7	\$250.3

The surplus of \$172.7 million is lower than the 2020 surplus of \$250.3 million, by (\$77.6) million or (31%). The change is primarily attributable to lower grant revenue and higher operating expenses with the completion of WTP and a number of Regional Housing First Program projects.

The increase in equity, reserves and operating funds represent the intended use of surplus to fund future capital, reserves and annual operating costs.

3. Other Financial Statement Analysis

Summaries and analysis of the remaining three statements can be found in Appendix C:

3. Statement of Changes in Net Debt;
4. Statement of Remeasurement Gains and Losses; and
5. Statement of Cash Flows

Financial Indicators

As in prior years, the consolidated financial health of the organization is monitored and reported through financial indicators (Appendix E). These measures demonstrate a consistent, healthy financial position based on operational needs, market conditions and debt servicing costs.

COVID-19 Impacts

An assessment was made by management regarding organizational impacts due to COVID-19. Overall, there was no significant financial impact in the 2021 fiscal year. Provincial health orders in place throughout 2021 impacted service levels at recreation centers but to a lesser degree than 2020. The impact on revenues were balanced through mitigation on costs balancing the service results in 2021.

In September 2020, the Province announced joint Provincial and Federal funding to support local government operations as part of BC's Economic Recovery Plan. The CRD received \$1.4 million in grants from this initiative in November 2020 and an additional \$0.6 million was received in March 2021. At the end of 2021 there remains \$0.3 million in unspent funds. The Unaudited schedules now include a schedule summarizing the funds received, services that received that funding and the ending balance.

Emerging Accounting Issues

Asset Retirement Obligations

As identified in Appendix 4 and page 12 of the Audit Findings Report (Appendix F), the upcoming asset retirement obligation change is a significant accounting standard that will be effective for the year ending December 31, 2023. The new standard addresses the recognition, measurement, presentation and disclosure of legal obligations associated with the retirement of tangible capital assets. It will require the CRD to record a liability in the financial statements related to future costs of any legal obligations to be incurred upon retirement of controlled tangible capital assets.

It is expected the introduction of the new accounting standards for asset retirement obligations will result in a significant revaluation of the landfill liability and recognition of all closure and post-closure costs. The standard will require the entire post-closure liability to be recorded upfront rather than over time as is currently done. The change in standard does not address or direct how the liability will be funded.

As staff begin preparing to implement the standard across all services, scope, timing and financial implications will be reported to the Board through Committee.

Public Private Partnerships

As identified in Appendix 4 of the Audit Findings Report (Appendix F), PSAB has developed a new accounting standard that provides requirements for recognizing, measuring and classifying infrastructure procured through a public private partnership (P3). The standard will be effective for the year ending December 31, 2024, with an option to early adopt.

This standard will apply to the Residuals Treatment Facility P3 agreement. Staff have taken steps to ensure that the recognition, measurement and disclosures relating to the agreement addresses many of the requirements under the incoming standard. Other work to be completed before adoption includes a scan of all infrastructure agreements to identify any other P3 arrangements which would be incorporated into reporting and disclosure upon adoption of the new standard.

CONCLUSION

Board approval of the CRD 2021 Statement of Financial Information is required under the *Local Government Act*, *Community Charter*, and *Financial Information Act*. As noted in the Audit Findings Report, it is the auditors' opinion that these financial statements present fairly the consolidated financial position of the CRD as of December 31, 2021, and the results of financial activities for the year then ended in accordance with Canadian Public Sector Accounting Standards.

RECOMMENDATION

The Finance Committee recommends to the Capital Regional District Board:
That the Capital Regional District 2021 Statement of Financial Information be approved.

Submitted by:	Rianna Lachance, BCom, CPA, CA, Senior Manager, Financial Services
Concurrence:	Nelson Chan, MBA, FCPA, FCMA, Chief Financial Officer
Concurrence:	Robert Lapham, MCIP, RPP, Chief Administrative Officer

ATTACHMENT(S)

- Appendix A: 2021 Statement of Financial Information
- Appendix B: 2021 Unaudited Statements
- Appendix C: 2021 Other Financial Statement Analysis
- Appendix D: DBRS Rating Methodology
- Appendix E: 2021 Additional Financial Analysis
- Appendix F: 2021 Audit Findings Report
- Appendix G: 2021 KPMG Management Letter