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**REPORT TO CAPITAL REGIONAL DISTRICT BOARD
MEETING OF WEDNESDAY, MAY 13, 2020**

SUBJECT **CRD 2019 Audit Findings Report and Statement of Financial Information**

ISSUE SUMMARY

To approve the Capital Regional District (CRD) 2019 Statement of Financial Information (SoFI) and receive the 2019 Audit Findings Report for information.

BACKGROUND

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

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

The audit has now been completed. The 2019 Audited Financial Statements have been prepared by management in accordance with Canadian Public Sector Accounting Board (PSAB) Standards. Under PSAB regulations, governments are required to present 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 to the required statements listed above, the 2019 Consolidated Statements of Financial Information (Appendix A) include:

6. Schedules of Long Term Debt
7. Schedule of Guarantee and Indemnity Agreements
8. Schedule of Supplies of Goods and Services
9. Schedule of Remuneration and Expenses – Directors
10. Schedule of Remuneration and Expenses – Employees
11. Statement of Severance

Also included in the package are unaudited statements (Appendix B) that present financial information for each service, a whitepaper on rating Canadian Municipal Governments (Appendix C) which describes DBRS's credit rating methodology, additional financial analysis (Appendix D)

that provides financial indicators on 2019 financial results, and the 2019 Audit Findings Report (Appendix E).

The audit findings report (Appendix E) summarizes the responsibilities of the audit firm, scope of investigations, and the audit results. The report highlights that the audit did not identify any uncorrected differences or significant control deficiencies. The report also confirms there were no significant changes in the audit approach from the Audit Planning Report presented to the Board on January 8, 2020.

ALTERNATIVES

Alternative 1

That the Capital Regional District 2019 Audit Findings Report be received and the Capital Regional District 2019 Statement of Financial Information be approved.

Alternative 2

That the Capital Regional District 2019 Audit Findings Report be received and the Capital Regional District 2019 Statement of Financial Information be referred back to staff for additional information.

IMPLICATIONS

Financial Implications

Audit Findings Report

The Auditor's opinion is included in the financial statements in Appendix E. In KPMG's opinion, the financial statements present fairly, in all material respects, the financial position of the Capital Regional District as at December 31, 2019 in accordance with Canadian public sector accounting standards.

The Audit Findings report provides the results of their audit, and reports results in areas of focus identified in the Audit Planning Report presented to Board on January 8, 2020. Also included in the report is a summary of corrected and uncorrected adjustments on pages 25 and 26.

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. The CRHC audited financial statements were presented and approved by the CRHC Board on April 22, 2020, and will be published on the CRD website.

HIGHLIGHTS

1. Consolidated Statement of Financial Position

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

- a. Cash resources,
- b. The net debt position calculated as the difference between 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. CRD financial assets are made up of cash, short and long term investments and debt. These assets are used to pay vendors and employees.

Cash and Cash Equivalents

Cash and cash equivalents includes cash on hand, bank deposits and cashable investments. The cash and cash equivalent balance increased in 2019 by \$114.4 million to \$184.5 million. The increase is attributable to more cash held in high interest savings accounts (HISA) versus fixed term deposits and higher grant revenue collected for capital projects. Further detail on changes in cash are discussed below in section 5, Consolidated Statement of Cash Flows.

Investments

Investments include term deposits of \$72.8 million and the MFA bond fund holdings of \$41.4 million. Investments decreased compared to 2018 by \$54.0 million. The reduction in investment balance is consistent with more cash held in higher yielding HISA's.

Accounts Receivable

Accounts receivable are due through the normal course of business and are net of doubtful accounts. The balance at year end will vary as a result of the timing of invoicing and payments. The decrease of \$1.9 million or 7.6% from prior year was due to receipt of \$1.0 relating to the Wastewater Treatment Project (WTP) and another \$1.0 million from Bike BC for trails.

Member Municipality Debt and Municipal Finance Authority (MFA) Debt Reserve Fund

Regional districts and municipalities are required to finance debt through the MFA. In the financial statements, debt recoverable from member municipalities is a receivable for their respective financing obligations, as such, there is no direct impact on CRD net debt. In 2019 member municipalities increased long term capital borrowings by \$13.7 million and repaid \$11.5 million, resulting in a net increase of \$2.1 million to \$153.0 million.

The debt reserve fund is the amount required to MFA as security for debt obligations issued to the District. These amounts are refundable, with interest, upon debenture maturity. Cash deposits of \$4.0 million (excluding member municipalities) are presented as a receivable on the financial statements. This balance fluctuates with debt issues and maturities.

Financial Liabilities

Liabilities are obligations or debt that will be settled through financial assets. Liabilities represent the costs for goods and services consumed and owed by the CRD. Liabilities are used to finance operations and large capital construction or acquisitions.

Accounts Payable and Other Liabilities

Collectively, accounts payable, deferred revenue and other liabilities increased by \$15.9 million, which is mainly due to a \$19.8 million increase in accounts payable related to WTP holdbacks. They are comprised mainly of:

- Amounts owing to suppliers for goods received and services rendered
- Deferred revenue, system development cost charges as an example
- Post-employment benefits and other benefits payable

Landfill Closure and Post-Closure Liability

The estimated liability increased by \$0.5 million, representing another year of capacity usage. The total liability represents the present value of the estimated future costs for closure and post closure obligations. Changes in the estimated costs, the useful life of the landfill, the discount rate and capacity estimates can have significant impacts on the recorded liability.

In 2019, an external review of the Hartland Landfill Master Filling Plan by Sperling Hansen Associates was completed, resulting in operational optimization and extension of the useful life. The revised filling plan is currently under public consultation as part of the Solid Waste Management Plan and once adopted will be result in a revised estimate.

Debt

Debt includes amounts for the CRD, CRHC and member municipalities, which increased by \$62.8 million to \$447.3 million. CRD and CRHC debt increased \$60.7 million in 2019 due to:

- \$145.0 million in borrowing for WTP, offset by a \$103.0 million pay down through grants;
- \$11.3 million pay down related to the sale of the Viewfield property; and
- \$35.5 million in borrowing for Millstream Ridge as part of the Regional Housing First Program.

Non-Financial Assets

Non-financial assets are resources held for service provision over one or more future periods such as tangible capital assets, inventories of supplies, prepaid portions of land leases, etc. Non-financial assets increased by \$283.6 million to \$1.5 billion in 2019, due mainly to an increase of \$233.7 million in work-in-progress additions for the Wastewater Treatment Project.

Accumulated Surplus

The accumulated surplus or net book value of equity for the CRD is \$1.4 billion, showing the organization has assets (Financial and Non-Financial) of greater value than what it owes (Liabilities). The equity can be summarized into the following categories:

Accumulated Surplus Categories:	\$ in Millions
Equity Invested in Tangible Capital Assets	1,243.5
Capital and Operating Reserves	137.8
Net Operating Funds	50.5
2019 Accumulated Surplus	1,431.8

The 2019 CRD net operating funds of \$50.5 million represents 4% of accumulated surplus and is an increase of \$34.3 million over 2018. The balance is predominantly in tangible capital assets, operating and capital reserves.

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.

The budget authorized by bylaw is included on the Statement of Operations and has been adjusted to exclude reserve transfers and principal repayment, and any other items not classified as expenses under PSAB standards. Other differences from budget exist but have not been adjusted as these did not form part of the original budget bylaw. These differences include grant revenue, deferred revenue, donations and amortization expense. Notable explanations pertaining to the Consolidated Statement of Operations are as follows:

Revenue

Revenue in 2019 increased by \$137.3 million or 46% to \$431.4 million. This was driven by:

- \$130.5 million increase in government transfers; \$27.9 million in federal and \$62.0 million of provincial grants for the WTP. There was also an additional \$30.0 million for the RHFP.
- \$2.5 million increase in other revenue; \$3.3 million pay down of developer contributions for the Skirt Mountain Reservoir offset by various accounts totaling \$0.8 million.
- \$2.3 million increase in affordable housing revenue; primarily driven by \$1.7 million in tenant rent as a result of completing Millstream Ridge which added 132 rental units.
- \$1.4 million increase in sale of services; primarily driven by a \$0.7 million increase in water sales in relation to growth in the region and water billing rates.
- \$1.4 million increase in interest earnings; a result of higher cash balances throughout 2019 when compared to 2018 and an active investment strategy.
- offset by a \$1.3 million decrease in developer contributions.

Expenses

Expenses in 2019 increased by \$12.5 million or 7.6% to \$177.2 million. This was driven by:

- \$4.4 million increase in salaries, wages and benefits; driven by contractual agreements, the employer health tax and benefit load costs.
- \$2.9 million increase in contract for services and consultants & repairs and maintenance; consistent with the CRD's overall increase in operational activity.
- \$1.4 million increase in interest on debt; directly correlated an increase in long term debt.

2019 Annual Surplus

The 2019 annual surplus is \$254.2 million, which identifies the change in accumulated surplus in the current year and is summarized in the table below:

Surplus Reconciliation	\$ in Millions
Operating surplus (final budget)	2.3
Add: Increase in Cap Equity	215.7
Add: Increase in Capital and Operating Reserves	3.8
Add: Increase in Operating Funds	34.3
All Other Eliminating/PSAB Entries	25.7
2019 Annual Surplus	254.2

The Operating surplus of \$2.3 million is 1% of annual budgeted revenues and driven by surpluses in General Government, Environmental Health Services including Landfill operations, Water Services and Sewer Services. This operating surplus is carried forward and used to offset 2020 requisition, fees and charges.

The \$215.7 million and \$3.8 million above are revenues and transfers to equity, restricted to funding current and future asset construction and acquisitions. As such, they are unavailable to moderate future requisitions. The increase in operating funds of \$34.3 million is used to fund ongoing operations in the coming year.

3. Consolidated Statement of Change in Net Debt

The Statement of Change in Net Debt reconciles current to prior year and informs the reader of change drivers. Included in this statement are expenditures that could be incurred in year but not consumed during the period; these include items such as tangible capital assets, inventory, prepaid expenses, and unrealized remeasurement losses on portfolio investments.

Overall, the net debt position increased by \$28.6 million driven by an increase of \$316.4 million of acquired and contributed capital assets, offset by the annual surplus of \$254.2 million, and amortization of \$31.6 million.

4. Consolidated Statement of Remeasurement Gains and Losses

Investments are carried at fair value and result in remeasurement gains or losses. The gains or losses remain unrealized until they are disposed, at which point they are recognized through the Statement of Operations.

There was \$0.1 million unrealized remeasurement gain was a result of an increase in market value of investments held in MFA bond fund and various term deposits. Additionally, the CRD divested ownership of the MFA Intermediate Fund resulting in \$0.7 million recognition into the Statement of Operations.

5. Consolidated Statement of Cash Flows

The Statement of Cash Flows reports the sources and uses of cash during the period, and provides information about capital, investing, and financing activities. Positive cash flow from operating activities represents core operations generating adequate cash operate, acquire new assets, and meet debt servicing costs. Capital activities resulted in negative cash flows, while investing and financing activities had positive cash flows. Overall, the CRD's cash position increased in 2019 by \$114.4 million.

The increase in cash was primarily driven by the annual surplus of \$254.2 million, which contributed to a \$296.4 million change in cash from operating activities. In addition, financing activities (long-term debt) increased cash by \$64.7 million, while investing activities increased \$54.9 million. Offsetting cash outflows were driven by capital activities of \$301.5 million.

Financial Indicators

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

Although overall net debt increased by \$28.6 million, debt ratios using the DBRS rating methodology demonstrate CRD is able to meet obligations and is unlikely to be adversely affected by future events. The debt increases are directly related to significant capital projects in the capital region in progress. These include, but are not limited to, the WTP and property acquisitions for the Regional Housing First Program. The overall 2019 revenue increased by \$137.3 million, demonstrating an expanded scope of CRD service delivery and grants received.

DBRS is Canada's largest and the world's fourth largest credit rating agency, respected for its independent, third-party evaluation of credit quality. They publish research whitepapers describing their methodology of rating Canadian municipal governments (Appendix C).

CONCLUSION

Board approval of the CRD 2019 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, 2019, and the results of financial activities for the year then ended in accordance with Canadian Public Sector Accounting Standards.

RECOMMENDATION

That the Capital Regional District 2019 Audit Findings Report be received and the Capital Regional District 2019 Statement of Financial Information be approved.

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

ATTACHMENT(S)

- Appendix A: 2019 Statement of Financial Information
- Appendix B: 2019 Unaudited Statements
- Appendix C: DBRS Rating Methodology
- Appendix D: 2019 Additional Financial Analysis
- Appendix E: 2019 Audit Findings Report
- Appendix F: 2019 KPMG Management Letter