

**Report to
Rapport au:**

**Audit Committee
Comité de la vérification
14 June 2018 / 14 juin 2018**

**and Council
et au Conseil
27 June 2018 / 27 juin 2018**

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Ward: CITY WIDE / À L'ÉCHELLE DE LA VILLE File Number: ACS2018-CSD-FIN-0015

SUBJECT: 2017 CITY OF OTTAWA CONSOLIDATED FINANCIAL STATEMENTS

OBJET: ÉTATS FINANCIERS CONSOLIDÉS DE 2017 DE LA VILLE D'OTTAWA

REPORT RECOMMENDATIONS

That the Audit Committee recommends Council approve the draft 2017 City of Ottawa Consolidated Financial Statements.

RECOMMANDATIONS DU RAPPORT

Que le Comité de la vérification recommande au Conseil d'approuver l'ébauche des états financiers consolidés de 2017 de la Ville d'Ottawa.

EXECUTIVE SUMMARY

Section 294 of the Municipal Act, 2001, requires that the City prepare annual audited consolidated financial statements in accordance with generally accepted accounting principles recommended by the Public Sector Accounting Board (PSAB) of the Chartered Professional Accountants of Canada (CPA Canada).

The Draft Consolidated Financial Statements (Document 1) have been prepared by management in accordance with Canadian Public Sector Accounting Standards established by PSAB of CPA Canada.

The City's external auditors Ernst & Young LLP have also provided their audit results to date and outlined steps for completion in the attached report (Document 2).

Financial Highlights

- Construction of the Confederation Line continued to be a significant item on the consolidated financial statements.
- Shift from longer term investments to cash to align with cash flow requirements for major City projects in 2018.
- Accounts receivable and government transfer revenue decreased as the Confederation Line Stage 1 is nearing completion.
- Accounts payable increased due to higher expenditures for Confederation Line combined with higher taxation remissions.
- Employee future benefits increased due to increases in long-term disability and health claims.
- Deferred revenue decreased due to more expenses now funded by development charges for the Confederation Line.
- Net long-term debt increased more than the previous year. The planned 2018 debt issue was advanced and combined with the 2017 new debt issuance to reduce the cost impact of increasing interest rates.

RÉSUMÉ

L'article 294 de la Loi de 2001 sur les municipalités exige que la Ville prépare des états financiers consolidés et vérifiés chaque année conformément aux principes comptables

généralement reconnus recommandés par le Conseil sur la comptabilité dans le secteur public (CCSP) de Comptables professionnels agréés du Canada (CPA Canada).

Les états financiers consolidés provisoires (document 1) ont été préparés par la direction conformément aux normes comptables du secteur public canadien, établies par le CCSP de CPA Canada.

Le vérificateur externe de la Ville, la société à responsabilité limitée EY, a aussi publié les résultats de la vérification et définit les étapes à réaliser dans le rapport ci-joint (document 2).

Faits saillants des états financiers

- La construction de la Ligne de la Confédération continue d'occuper une place importante dans les états financiers consolidés.
- La Ville troque les investissements à long terme contre les liquidités pour répondre aux besoins de trésorerie des grands projets municipaux en 2018.
- Les comptes débiteurs et les paiements de transfert ont diminué en raison de l'achèvement prochain de la construction de l'Étape 1 de la Ligne de la Confédération.
- Les comptes créditeurs sont en hausse en raison d'une augmentation des dépenses pour la Ligne de la Confédération ainsi que d'une augmentation des remises de taxes.
- Les avantages sociaux futurs des employés ont augmenté en raison d'une hausse des réclamations en invalidité de longue durée et des demandes de remboursement de frais médicaux.
- Les revenus reportés ont diminué en raison d'une hausse des dépenses maintenant financées par les redevances d'aménagement pour la Ligne de la Confédération.
- Le passif à long terme de la Ville a connu une hausse supérieure à celle de l'an passé. L'émission obligataire prévue pour 2018 a été devancée et combinée aux nouveaux titres de créance émis en 2017, afin de réduire l'incidence financière de la hausse des taux d'intérêt.

BACKGROUND

Section 294 of the *Municipal Act, 2001*, requires that the City prepare annual audited consolidated financial statements in accordance with generally accepted accounting principles recommended by PSAB of CPA Canada. These audited financial statements must be made available to the public.

On November 30, 2017, Ernst & Young LLP provided an audit plan ([ACS2017-CSD-FIN-0029](#)), outlining the scope of key issues affecting the 2017 audit for the information of Committee and Council.

DISCUSSION

The consolidated financial statements have been prepared by management in accordance with Canadian Public Sector Accounting Standards established by PSAB of CPA Canada. These accounting policies require the reporting of revenues and expenses on an accrual basis of accounting. The accrual basis of accounting recognizes revenues and expenses, as they are incurred and measurable as the result of the receipt of goods and services.

These consolidated financial statements include the operation of all local boards and agencies, such as the Police Services Board, Ottawa Public Library Board, the Ottawa Community Housing Corporation, and the Business Improvement Areas. The City's investment in Hydro Ottawa is recorded in the consolidated financial statement on a modified equity basis.

Consolidated Financial Statements

The consolidated financial statements are comprised of four individual statements and detailed notes to the consolidated financial statements:

The Consolidated Statement of Financial Position focuses on the City's assets (financial and non-financial) and liabilities. The difference between the liabilities and the financial assets is the City's net debt, which represents the liabilities that must be financed from future revenues.

The Consolidated Statement of Operations and Accumulated Surplus outline the revenue, expenses, surplus, and changes in accumulated surplus for the year. It includes the combined financial activity of the operating, capital, and reserve funds of the City and its consolidated entities.

The Consolidated Statement of Change in Net Debt outlines the changes in net debt as a result of annual operations, tangible capital asset transactions, and changes in other non-financial assets.

The Consolidated Statement of Cash Flows summarizes the City's cash position and changes during the year based on sources and uses of cash.

Key Terms

It is important to highlight some key terms used in the consolidated financial statements from an accounting perspective, which differ from similar terms used from a budgeting perspective.

Accruals: The consolidated financial statements are prepared using the accrual basis of accounting which records expenses and revenues which the City expects to expend or receive cash in a future reporting period.

Financial assets are assets that could be used to discharge existing liabilities or finance future operations and are not for consumption in the normal course of operations.

Liabilities represent obligations that must be paid over the short and long term. Liabilities include accounts payable and accrued liabilities, deferred revenue, employee future benefits and pension agreements, environmental liabilities for landfill closure/post closure and contaminated sites and liabilities for debt obligations including mortgages and capital lease obligations.

Net debt is the difference between financial assets and liabilities. It is a measure of the future revenues required to pay for past transactions.

Non-financial assets are comprised primarily of tangible capital assets which include roads, water and waste-water infrastructure, buildings and improvements, land, machinery, plant and equipment, vehicles, and assets under construction. Tangible capital assets represent the largest item on the City's Consolidated Statement of Financial Position. As tangible capital assets do not provide liquidity, and are generally used to deliver government services, they are reported separately with inventories and prepaid expenses, as Non-financial assets.

Annual Surplus is reported on the Consolidated Statement of Operations. Annual surplus represents the difference between the revenue and expenses of the City from an accrual accounting perspective.

Accumulated Surplus essentially is the overall equity. It represents the net of all the City's assets (financial and non-financial) and liabilities. These assets are available to service future generations.

Reserves comprise funds set aside for specific purposes by Council and are a component of Accumulated Surplus. Amounts received for specific purposes under

legislation, regulation or agreement such as development charges represent a liability and are reported as Deferred Revenue and not Accumulated Surplus.

Operating and Capital Budgets

The City's Operating and Capital Budgets are based upon a modified cash basis of accounting. This results in significant differences between the City's external financial statements and its Operating and Capital Budgets. PSAB accounting policies require that the consolidated financial statements show a comparison of the actual financial results for the period to those originally planned (budgeted). These policies also state that those "planned" (budgeted) results should be presented for the same scope of activities and on a basis consistent with that used for actual results. Since the City prepares its Operating and Capital budgets on a different basis from that used to account for transactions in the consolidated financial statements, it is necessary to provide a reconciliation of Council's approved budgets to the budget figures reported in the financial statements. This reconciliation is provided in Note 21 to the consolidated financial statements.

The City uses cash accounting for budgeting because it is the most accurate way of determining how much taxation needs to be levied in any one year. It is the cash requirement that determines what the tax rate is and also what tax rate increase may be required. The accrual basis of accounting used in the consolidated financial statements includes expenses that do not need to be financed or tax levied for in the immediate near term. An example is the future cost of closing landfill sites.

Table 1 Consolidated Statement of Financial Position (in thousands \$000)

	2017	2016
Financial Assets		
Cash and cash equivalents	383,259	257,124
Accounts receivable	510,621	607,222
Investments	1,237,136	1,273,376
Investment in government business enterprise	438,190	426,795
Total financial assets	2,569,206	2,564,517
Liabilities		
Accounts payable and accrued liabilities	1,219,317	1,124,366

Deferred revenue	482,619	564,273
Employee future benefits and pension agreements	621,390	595,152
Environmental liabilities	34,431	34,050
Net long-term debt	2,032,895	1,710,431
Other liabilities	397,862	369,262
Total liabilities	4,788,514	4,397,534
Net Debt	(2,219,308)	(1,833,017)
Non-Financial Assets		
Tangible capital assets	15,340,462	14,494,891
Other non-financial assets	60,673	62,650
Total non-financial assets	15,401,135	14,557,541
Accumulated Surplus	13,181,827	12,724,524

Analysis of the Consolidated Statement of Financial Position

In 2017, there was a continued shift from long-term investments to cash and cash equivalents to take advantage of increases in short term lending rates, and to align with cash flow requirements for major City projects including the Confederation Line in 2018.

The decrease of \$97 million in accounts receivable is net of a decrease totalling approximately \$135 million for receivables from the federal and provincial government. The bulk of this decrease relates to lower receivables for the final stages of construction of the Confederation line. These decreases were offset by increases of approximately \$26 million for taxes and user charges and approximately \$12 million for trade receivables.

The investment in government business enterprise, which represents the net value of Hydro Ottawa, increased by \$11 million. This increase represents the net of the City's share of Hydro Ottawa income of approximately \$32 million and dividends paid of \$21 million.

Accounts payable and accrued liabilities increased approximately \$95 million in 2017 and is net of increases of approximately \$105 million in accounts payable and decreases of approximately \$10 million for accrued liabilities. Increases in accounts payable include additional payables at the end of the year for the Confederation Line of

\$52 million. Taxation payables increased approximately \$33 million and is net of higher payables for remissions of \$42 million and lower payables related to the phase out of the vacancy rebate program of \$9 million. In 2017, the Assessment Review Board (ARB) introduced changes in legislation for remissions to accelerate the settlement of open appeals and reduce backlog. Accrued liabilities decreased by approximately \$10 million due to timing differences in scheduled pay and other employee costs.

Deferred revenue decreased by approximately \$82 million mainly due to lower development charges. Development charge receipts are recorded as deferred revenue until the fiscal year when the related expenses are incurred at which point they are recorded as revenue. In 2017, there was an increase in expenses for the Confederation Line funded by development charges, which resulted in matching increased revenues and a reduction in deferred revenue.

Employee future benefits and pension agreements increased by approximately \$26 million. Employee future benefits include increases of \$27 million due to an increase in long-term disability claims associated with mental health and an increase in back and shoulder claims and a \$6 million increase in post retirement benefits. Employees are retiring at an older age and are requiring more health benefits. These liabilities were partially offset by a \$7 million reduction in the liability for the City of Ottawa Superannuation Fund.

The City's environmental liabilities include liabilities for landfill closure and post-closure and contaminated sites. The landfill closure and post-closure liability increased by \$0.5 million in 2017 based on revised estimates to cap two inactive landfill sites in the future. This increase was partially offset with a decrease in the liability for contaminated sites of approximately \$0.2 million due to the disposal of four properties.

Net long-term debt increased by approximately \$322 million reflecting the difference between \$432 million of new debt issues and \$110 million of debt principal repayment.

The growth in tangible capital assets is due primarily to continued spending on the Confederation Line including preliminary work for Phase 2, which accounted for approximately \$510 million of the total \$845 million.

Accumulated surplus increased by \$457 million and is net of increases in the City's investment in tangible capital assets of \$367 million, increases in reserves of \$114 million, and the city's investment in Hydro Ottawa of \$11 million offset by increases in unfunded liabilities of \$30 million and a \$5 million decrease in the City's Endowment Fund.

The growth in the City's reserves is due to the closing out of the City's capital projects, additional funds generated from refinancing mortgages for Ottawa Community Housing Corporation, and growth in gas tax reserves to be used in future years.

Table 2: Analysis of Key Accounts Consolidated Statement of Operations and Accumulated Surplus – Revenue (in thousands \$000)

Revenue	2017 Budget	2017 Actual	2016 Actual
Taxes	1,721,599	1,703,630	1,653,541
Government transfers	674,785	683,114	907,057
Fees and user charges	831,331	819,865	809,540
Contributed tangible capital assets	205,693	205,693	182,296
Development charges	217,076	217,076	121,851
Investment income	34,080	37,778	37,721
Fines and penalties	28,412	34,168	31,618
Other revenue	35,760	51,214	33,579
Share of earnings of government business enterprise	35,375	35,975	34,836
Total Revenue	3,784,111	3,788,513	3,812,039

The largest source of revenue is property tax revenue at 44 per cent, while fees/user charges and government transfers represent 22 per cent and 18 per cent, respectively of the total consolidated revenue.

Taxation revenue increased by \$50 million to \$1.704 billion (2016 - \$1.654 billion). This increase is net of a tax levy increase of approximately \$56 million and higher supplementary assessments of \$6 million offset by higher remissions of \$12 million. The tax levy increase includes a 2 per cent overall property tax bill increase amounting to \$35 million combined with a \$21 million increase in the assessment base due to new properties.

Government transfer revenue decreased by \$224 million to \$683 million (2016 - \$907 million). Lower revenues for the Confederation Line Stage 1 accounted for a decrease of \$260 million. This decrease was offset with a \$21 million increase in funding for social assistance due to increased caseloads and new funding for social housing programs of \$15 million.

Fees and user charge revenue increased by \$10 million to \$819 million (2016 - \$809 million). This was partly due to increases of approximately \$5 million for waste and recycling growth. Rate increases for water, sewer surcharge and transit fares contributed to the balance of the increase.

Contributed tangible capital assets represent assets that are donated or contributed to the City by developers. In 2017 contributed assets increased by approximately \$23 million to \$205 million (2016 - \$182 million).

Development charges applied to capital spending increased by \$95 million to \$217 million (2016 - \$122 million). Development charge revenue is not recognized until the funds are spent for its intended purposes. The increase reflects the shift to more funding coming from development charges in the later stages of construction for the Confederation Line, while government funding primarily funded the earlier stages.

Fines and penalties increased in 2017 by \$2 million to \$34 million (2016 - \$32 million). This was due to the higher late payment penalties and higher collections for provincial offences.

Other revenue increased by \$17 million to \$51 million in 2017 (2016 - \$34 million) due to proceeds from the sale of land administered by the city's wholly owned land corporation.

Share of earnings of government business enterprises increased to \$36 million in 2017 (2016 - \$35 million).

Table 3: Analysis of Key Accounts Consolidated Statement of Operations and Accumulated Surplus – Expenses (in thousands \$000)

Expenses	2017 Budget	2017 Actual	2016 Actual
General government	103,560	98,821	95,687
Protection to persons and property	564,648	563,103	578,309
Roads, traffic and parking	397,100	410,761	413,504
Transit	566,440	554,548	560,099
Environmental services	384,004	368,356	381,763
Health services	176,029	177,062	162,164
Social and family services	472,105	484,138	457,850
Social housing	280,738	270,532	273,291

Recreation and cultural services	335,082	329,542	316,348
Planning and development	74,837	70,367	69,538
Total Expenses	3,354,543	3,327,230	3,308,553

General government expenses increased by \$3 million to \$99 million in 2017 (2016 - \$96 million).

Protection to persons and property decreased by \$15 million in 2017 to \$563 million (2016 - \$578 million) due to lower WSIB costs compared to 2016. Provincial legislation deeming cancer as work related caused a significant increase in 2016.

Roads, traffic and parking expenses decreased by \$3 million to \$411 million in 2017 (2016 - \$414 million).

Environmental services decreased by \$14 million in 2017 to \$368 million (2016 - \$382 million) mainly due to reduced repair and maintenance costs in 2017 compared to 2016.

Health services increased by \$15 million to \$177 million in 2017 (2016 - \$162 million) mainly due to additional staffing and supplies associated with ambulance call volume and higher employee future benefits costs.

Social and family services increased by \$26 million to \$484 million in 2017 (2016 - \$458 million) due to higher caseload volumes combined with changes in provincial legislation for childcare allocation.

Recreation and Cultural Services increased by \$13 million to \$329 million in 2017 (2016 - \$316 million) due to an increase in repairs and maintenance to recreational facilities compared to 2016.

External Audit

The City's external auditors have performed an audit of the Draft Consolidated Financial Statements. Under accounting standards, the City's external auditors are required to extend their subsequent events review procedures up until Council approves the Draft Consolidated Statements. These audit procedures include the review of bank statements, payments and receipts in the subsequent period as well as additional standard inquires. In order to reduce the amount of post audit review, this report should be brought for Council's review at the earliest opportunity. Once Council approves the Draft Consolidated Statements, the City will receive the signed audit report at which time the statements will be considered final and be posted on the City's web site.

Financial Information Return

The City also prepares a financial information return for submission to the Province of Ontario, based on the financial results contained in the consolidated financial statements. That information is also available publicly through the Province's financial information web site.

RURAL IMPLICATIONS

There are no rural implications associated with this report.

CONSULTATION

This report is administrative in nature and consultation is not applicable.

COMMENTS BY THE WARD COUNCILLOR(S)

This report is administrative and city wide in nature.

ADVISORY COMMITTEE(S) COMMENTS

Not applicable.

LEGAL IMPLICATIONS

There are no legal impediments to approving the recommendations in this report.

RISK MANAGEMENT IMPLICATIONS

There are no risk implications.

ASSET MANAGEMENT IMPLICATIONS

There are no asset management implications.

FINANCIAL IMPLICATIONS

Financial implications are outlined in the body of this report.

ACCESSIBILITY IMPACTS

The City of Ottawa must comply with the Accessibility for Ontarians with Disability Act, 2005 ("AODA") in particular the Accessibility Standards for Customer Service, O. Reg. 429/07 as well as the Integrated Accessibility Standards, O. Reg. 191/11.

ENVIRONMENTAL IMPLICATIONS

There are no environmental implications to this information report.

TERM OF COUNCIL PRIORITIES

This report meets Council's priority with respect to financial responsibility.

SUPPORTING DOCUMENTATION

Document 1 – Draft 2017 City of Ottawa Consolidated Financial Statements

Document 2 - Ernst & Young Audit Results, Consolidated Financial Statements

DISPOSITION

Once Council approves the Draft Consolidated Statements, the City will receive the signed audit report at which time the statements will be considered final and be posted on the City's web site.