VAUGHAN

memorandum

COMMUNICATION – C1
Council – September 29, 2020
Committee of the Whole
Report No. 40, Item 1

DATE: September 23, 2020

TO: Honourable Mayor and Members of Council

FROM: Michael Coroneos, Deputy City Manager of Corporate Services, City Treasurer and CFO

RE: **Committee of the Whole (2) – September 22, 2020 – Amendment to Item#1 2019 Draft Consolidated Financial Statements – Attachment 3**

Please find attached a replacement Attachment 3, to the 2019 Draft Consolidated Financial Statements – Item 1, Committee of the Whole (2) on September 22nd.

KPMG has changed their Audit Findings Report to remove the word “consider” from their discussion on page 10 of Employee Future Benefits as a result of a discussion at the Committee of the Whole (2) meeting on September 22nd, 2020.

The sentence now reads, “We believe management’s process for identifying and accounting for estimates is adequate.”

The corrected Attachment 3 should be received for information at the September 29th Council meeting.

Michael Coroneos,
Deputy City Manager Corporate Services, City Treasurer and CFO

The Corporation of the City of Vaughan

Audit Findings Report
for the year ended December 31, 2019

KPMG LLP

Licensed Public Accountants

Prepared August 19, 2020

Presented September 22, 2020

kpmg.ca/audit

KPMG

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Executive summary

Purpose of this report[1]

The purpose of this Audit Findings Report is to assist you, as a member of the Committee of the Whole (2), in your review of the results of our audit of the consolidated financial statements of the Corporation of the City of Vaughan (the “City” or the “Entity”) for the year ended December 31, 2019.

Changes from the Audit Plan

The significant changes from our audit plan resulted from COVID-19, which impacts the City’s operations subsequent to December 31, 2019. As a result of the pandemic, our audit approach and plan was adjusted to incorporate additional elements, testing and discussions with management, as well as the way in which we conducted our audit. The timing of the year-end audit took place in July. Subsequent events were assessed as part of our audit. See pages 4 and 15.

There have been no other significant changes.

Finalizing the Audit

As of the date of this report, we have completed the audit of the financial statements, with the exception of certain remaining procedures, which include amongst others:

- Completing our discussions with the Committee
- Completing subsequent events procedures, up to the date of approval of the financial statements, including receipt of the final legal enquiry letter
- Receipt of the signed management representation letter (dated upon City Council approval of the financial statements)
- Obtaining evidence of City Council’s approval of the financial statements

We will update the Committee, and not solely the Chair, on significant matters, if any, arising from the completion of the audit, including the completion of the above procedures. Our auditors’ report will be dated upon the completion of any remaining procedures.

Financial statement presentation and disclosure

The presentation and disclosure of the consolidated financial statements are, in all material respects, in accordance with the City’s relevant financial reporting framework, Canadian public sector accounting standards.

[1] This Audit Findings Report should not be used for any other purpose or by anyone other than the Committee of the Whole (2), City Council, and Management of the Entity. KPMG shall have no responsibility or liability for loss or damages or claims, if any, to or by any third party as this Audit Findings Report has not been prepared for, and is not intended for, and should not be used by, any third party or for any other purpose.

Executive summary (continued)

Significant accounting policies and practices

There was no change to the significant accounting policies during the year.

The City adopted a new public sector accounting standard in 2019. See page 14 for considerations regarding the implementation of the new standard in the current year financial statements.

Adjustments and differences

We did not identify differences that remain uncorrected.

We did not identify any adjustments that were communicated to management and subsequently corrected in the financial statements.

See page 16 for additional information.

Control and other observations

We did not identify any control deficiencies that we determined to be significant deficiencies in internal control over financial reporting. We do, however, provide our observations and recommendations on best practices on page 18.

Accounting estimates

Overall, we are satisfied with the reasonability of accounting estimates.

The areas of estimates relate to the carrying value of tangible capital assets, provisions for certain accrued liabilities, including obligations related to employee future benefits and provisions for liabilities arising from legal claims.

See pages 10 and 11.

We believe management's process for identifying critical accounting estimates for these balances to be adequate. We did not identify any indicators of possible management bias.

Accounting estimates are disclosed as such in note 1(o) to the financial statements.

Financial impact of COVID-19

We have discussed the impact of COVID-19 on the operations of the City with management. Due to the uncertainty of the future financial impact to the City, management has added a subsequent event to the notes to the financial statements. See page 15 for additional information.

See also page 4 for considerations in our audit and for resources.

Materiality

Materiality determination	Comments	Group amount
Materiality	Determined to plan and perform the audit and to evaluate the effects of identified misstatements on the audit and of any uncorrected misstatements on the financial statements. The corresponding amount for the prior year's audit was $17,000,000.	$17,000,000
Benchmark	Determined during our planning stage, and based on prior year total revenues as an estimate for revenue. This benchmark is consistent with the prior year.	$863,000,000
% of Benchmark	This is within the acceptable range of 0.5 to 3%. The corresponding percentage for the prior year's audit was 2%.	2%
Audit Misstatement Posting Threshold (AMPT)	Threshold used to accumulate misstatements identified during the audit. The corresponding amount for the prior year's audit was $850,000.	$850,000
Significant Component Statutory Audit Materiality:		**Amount**
VHI	Materiality for the audit of VHI, determined to be within the City of Vaughan's group audit requirements. The corresponding amount for the prior year's audit was $8.6M.	$5,500,000
Alectra	Group Materiality for the audit of Alectra. Alectra materiality specific to the City of Vaughan group audit – 20.5%. The corresponding amounts for the prior year's audit was 21.49% and $9,240,000.	$49,000,000 $10,045,000

Materiality is used to scope the audit, identify risks of material misstatements and evaluate the level at which we think misstatements will reasonably influence users of the financial statements. It considers both quantitative and qualitative factors.

To respond to aggregation risk, we design our procedures to detect misstatements at a lower level of materiality.

We have reported to the Committee:

- Corrected audit misstatements
- Uncorrected audit misstatements

See page 16.

Audit Response to COVID-19 Pandemic

COVID-19 was a key consideration in our audit approach for the December 31, 2019 financial statements.

Audit implications

Planning and risk assessment

- We obtained an understanding of the actual and potential financial reporting impacts, the changes in environment, and their impact on our:
  - identified and assessed risks of material misstatement
  - audit strategy, including the involvement of others and the nature, timing and extent of tests of controls and substantive procedures

Executing

- We performed a remote audit in July, which included increased use of collaboration tools.
- Increased use of electronic evidence (and understanding the Entity's processes to provide such evidence to us)

Enhanced considerations

- We discussed any financial implications and actions undertaken by the City with management in relation to COVID-19, including:
  - Events or conditions that cast significant doubt regarding going concern and other indicators of financial distress
  - Impairment of non-financial assets (e.g., tangible capital assets)
  - Impairment of financial assets (e.g., financial instruments, such as investments and receivables)
  - Provisions and contingencies

Subsequent event considerations

Subsequent to year-end, the COVID-19 outbreak was declared a pandemic by the World Health Organization and has had a significant financial, market, and social dislocating impact. As such, enhanced subsequent event procedures are warranted.

There are two types of subsequent events, with the accounting treatment dependent on the categorization as follows:

- Events that provide future evidence of conditions that existed at the financial statement date. For these conditions, the financial statements should be adjusted for measurable impact to the assets, liabilities, revenues and expenditures.
- Events that are indicative of conditions that arose subsequent to the financial statement date. For these conditions, disclosures, at a minimum, should include a description of the event and an estimate of the financial impact, when practicable, or a statement that an estimate cannot be made.

We discussed the types of subsequent events with management and the impact on the City's financial statement disclosures. A subsequent event note disclosure is included in note 17(a) to the financial statements.

Potential financial reporting implications

Refer to our COVID-19 Financial Reporting site for considerations of potential ongoing impacts to financial reporting.

Resources

COVID-19 Alerts (Live Link)

Please visit our COVID-19 website for resources regarding operational topics, including tax, legal and business continuity considerations. This site is being updated daily based on information being released by Federal, Provincial and Municipal news releases.

Audit risks and results

We highlight our significant findings in respect of significant financial reporting risks.

1	Significant Risk	Fraud risk from revenue recognition

Significant financial reporting risk	Why is it significant?
Fraud risk from revenue recognition.	This is a presumed fraud risk, as required under our professional auditing standards. The primary risk of fraudulent revenue recognition resides with manual journal entries for revenue transactions not in the normal course of business as well as management's calculation of the deferred revenue – obligatory reserve funds balance.

Our response and significant findings

In order to address the presumed fraud risk from revenue recognition, we performed various audit procedures over the City's process for recognizing contributions from developers revenue, including:

- Evaluated the design and implementation and tested the operating effectiveness of selected relevant controls, including those relating to the tracking and reporting of capital project expenditures, and approvals of journal entries.

Other audit procedures included:

- Tested journal entries that are susceptible to manipulation through management override and unusual journal entries. See further details on page 12.
- As part of our audit approach to address the inherent risk of error in revenue recognition, we substantively tested revenues (both recognized and amounts held as deferred at year end) and analyzed unspent obligatory reserve funds through auditing management's methodology.
- Substantively tested development charges and other obligatory reserves cash receipts.
- Obtained the deferred revenue, obligatory reserve fund continuity schedule and selected samples for testing to determine if the original development charges received in prior years were used to fund capital expenditures in the current year and in accordance with the appropriate legislation. Based on our procedures, we conclude that the development charges recorded as revenue in fiscal 2019 were used to fund eligible capital projects.
- Reviewed recognition considerations for the other revenue streams.

We did not identify any issues related to fraud risk associated with revenue recognition.

Audit risks and results

2	**Significant Risk**	Fraud risk from management override of controls

Significant financial reporting risk	Why is it significant?
Fraud risk from management override of controls.	This is a presumed fraud risk, as required under our professional auditing standards. We have not identified any specific additional risks of management override relating to this audit.

Our response and significant findings

As the risk is not rebuttable, our audit methodology incorporates the required procedures in professional standards to address this risk. These procedures include testing of journal entries and other adjustments, performing a retrospective review of estimates, as relevant, and evaluating the business rationale of significant unusual transactions.

Professional standards require certain procedures to be performed to address the presumed risks of management override of controls.

– Using our Data & Analytics software, we tested manual and automated journal entries by extracting all journal entries recorded in the general ledger system and other adjustments. Using these extractions, we selected a sample of journal entries and verified if they were supported by proper documentation and followed the journal entry initiation and approval controls and process in place. We did not find any exceptions in our testing over journal entries. Please see page 12 for details and results.
– Evaluated the completeness of the journal entry population through a roll-forward of all general ledger accounts.
– We evaluated the reasonableness of estimates. We found that management's process for identifying accounting estimates is considered adequate.
– We did not identify any specific additional risks of management override during our audit.

We did not identify any issues related to fraud risk associated with management override of controls.

Other areas of focus

Significant findings from the audit regarding areas of focus are as follows:

3	Area of focus	Vaughan Holdings Inc.

Other area of focus

- We assessed Vaughan Holdings Inc. (“VHI”) as a significant component of the City’s consolidated financial statements.

Our response and significant findings

- The City recognizes its investment in Hydro Vaughan Corporations using the modified equity method. Using the criteria under Public Sector Accounting Standards (“PSA Standards”) PS 3070 – Investment in Government Business Enterprises, we determined that the City’s investment in Hydro Vaughan Corporations continues to meet the criteria of the standard, and therefore it is appropriate to continue to record the investment using the modified equity method of accounting.
- In 2019, the City’s share of Hydro Vaughan Corporations’ net income and dividends paid out totalled $10.8M and $14.3M, respectively (2018 - $25.2M and $12.7M, respectively).
- VHI received a $1.9M (2018 - $2.2M) return of capital from Alectra, which was recorded as a reduction to VHI’s investment in Alectra. VHI issued a similar return of capital of $1.9M to the City.
- On January 1, 2019, Alectra amalgamated with Guelph Hydro Electric Systems Inc. As a result of the amalgamation, VHI’s investment in Alectra effectively changed from 21.49% to 20.5% and also resulted in a net gain to the City, through VHI, of $989.6K.
- These transactions are described in note 4 to the financial statements.
- We verified the transactions between each of the respective entities, and performed a reconciliation of the amounts reported in the financial statements of the City, VHI, and Alectra as at December 31, 2019.
- **Based on our audit, we conclude that management has appropriately recorded and presented its investment in Hydro Vaughan Corporations using modified equity accounting.**

Other areas of focus

4	Area of focus	YMCA Project

Other area of focus

- In 2017, the City entered into an arrangement with YMCA of Greater Toronto Area (“YMCA”) and Penguin Calloway Vaughan Partnership for the construction of a YMCA and City Facility (together, “facility”) that is within a mixed use building being developed in the Vaughan Metropolitan Centre. The City is funding a significant portion of the construction costs and is guarantor to the YMCA’s share of financing.

Our response and significant findings

- The facility will be shared between the City and YMCA for occupancy whereby the City will use 30% of the facility and YMCA will use the remaining 70%.
- The City is funding its 30% share of the facility and 2/3 of YMCA’s 70% share of the facility.
- YMCA entered into a financing agreement with Ontario Infrastructure and Lands Corporation (OILC) to obtain a construction loan of up to $66M, which the City has guaranteed. In the event of default by YMCA, the City is required to assume all liabilities and take first right to ownership of all assets related to the facility, as part of this transaction.
- As at December 31, 2019, the City has incurred a cumulative $53.0M (2018 - $40.5M) on the project, comprising:

(millions)	2019	2018
Land	$11.0	$11.0
Land transfer tax	1.5	1.5
The City’s portion of the facility	15.6	10.8
The YMCA’s portion of the facility	24.9	17.2
	$53.0	$40.5

- The City has reported the $53.0M (2018 - $40.5M) as assets under construction as part of its tangible capital assets. A total of $11.4M (2018 - $11.4M) has been paid by the City with a remainder of $41.6M (2018 - $29.3M) recorded as long-term debt.
- These transactions are described in note 7 to the financial statements, including the repayment schedule of debt payments owing to YMCA.
- We obtained and reviewed relevant agreements related to this facility between the City and other parties. We reviewed the detail of costs related to this facility that were incurred during 2019. We obtained direct confirmation from YMCA of the long term debt and repayment schedule owing to them, including confirmation that YMCA has not defaulted on their loan with OILC as at December 31, 2019, and confirmed with management subsequently up to the date of this report.
- **We did not note any issues with management’s estimates and assumptions and we find the measurement and disclosures related to this project to be appropriate.**

Other areas of focus

5	Area of focus	Municipal Accommodation Tax

Other area of focus

- Municipal Accommodation tax revenue (MAT) is a new revenue source for the City in 2019.
- The City incorporated a new municipal services corporation called Tourism Vaughan Corporation to carry out tourism promotion activities using 50% of MAT revenue.

Our response and significant findings

- The Municipal Act allows a local municipality to impose a transient accommodation tax and the City has done so by passing By-Law 029-2019, which, effective April 1, 2019, requires accommodation providers to charge a 4% municipal accommodation tax. For the 2019 year, the total amount recorded as revenue of the City is $2.1M.
- In May 2019, Tourism Vaughan Corporation was incorporated. 50% of MAT revenues collected by the City is transferred to Tourism Vaughan, with the business objective of tourism promotion in the city of Vaughan. Expenses related to such tourism promotion activities are recorded as expenses of Tourism Vaughan, unless shared expenses are mutually beneficial to the City, in which case, the costs are allocated between the two entities.
- As Tourism Vaughan is controlled by the City, its accounts are consolidated with the City and reported in the consolidated financial statements.
- The remaining 50% of MAT revenues retained, and unspent, by the City, are maintained in a discretionary reserve fund with a balance of $865K at the end of 2019.
- We selected a sample of revenues and tested their collections to cash receipts and remittance forms submitted by accommodation providers. We also tested expenses by sampling expenses and testing selected items to invoices and other supporting documentation.
- **We did not note any issues with municipal accommodation tax revenue or amounts reported in the Tourism Vaughan Corporation financial statements.**

Other areas of focus - estimates

6	Area of focus	Employee Future Benefits

Other area of focus

- There is estimation uncertainty due to assumptions and estimates used by the actuary in calculating the liability for Employee Future Benefits.
- Management is required to disclose information in the financial statements about the assumptions it makes about the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to carrying amounts of assets and liabilities within the next financial year.
- We believe management's process for identifying and accounting for estimates is adequate.

Our response and significant findings

- Employee future benefits provided by the City, which will require funding in future periods, include post-retirement non-pension benefits and WSIB.
- The post-retirement non-pension benefits include certain health, dental and life insurance benefits for retired employees. WSIB benefits include benefits under the Workplace Safety and Insurance Board Act.
- The liability of these future benefits has been determined by two separate actuarial valuations performed as at January 1, 2017 for the 3 years of 2017 to 2019:
  - **Post-retirement non-pension benefits**
  - **WSIB**
- Our procedures included an assessment of management's estimates and assumptions used in determining the valuation of the liability, including management's best estimates over inflation rate, discount rate, benefit cost trend rates, retirement age and expected average remaining service life.
- We obtained written confirmation from management's experts (the actuaries), and performed an evaluation of the competence, capabilities, and objectivity of the actuaries, as required by professional standards when using their work as audit evidence.
- We recalculated the accruals based on the information noted above and did not identify any discrepancies.
- The details related to employee future benefits are described in note 5 to the financial statements.
- **We did not note any issues with management's estimates and assumptions and we find the measurement and disclosures of post-retirement non-pension benefits and WSIB liability to be appropriate.**

Other areas of focus - estimates

7	Area of focus	Contingencies

Other area of focus

- There is estimation uncertainty related to the likelihood and measurement of a contingent liability.

Our response and significant findings

- PS3300 Contingent Liabilities requires that the City recognize a liability when it is likely that a future event will confirm that a liability has been incurred at the date of the financial statements; and the amount can be reasonably estimated.
- At any point in time, the City is subject to a number of matters which could potentially result in the determination of a contingent liability as defined above, including, but not limited to, matters such as legal claims, potential contamination of City-owned sites, etc.
- We reviewed the City's assessments of contingent liabilities and the process employed to develop and record the related estimated liabilities. Where applicable, KPMG discussed with the individuals responsible for the process and is satisfied that the methodology used is rational, consistent with the approach taken in prior years and has been appropriately reviewed.
- As these items are resolved, it is possible that the final amounts recorded for these liabilities may change, however the amounts currently recorded represent management's best estimates of exposure given the information presently available.
- **We did not note any issues in the City's assessment of contingent liabilities and amount of related liabilities that were recorded and reported for the year-ended December 31, 2019.**

Technology in the audit

We have utilized technology and D&A to enhance the quality and effectiveness of the audit.

Tool	Our results and insights
Journal entry testing	We utilized our proprietary D&A tool, IDEA, to evaluate the completeness of the journal entry population through a roll-forward of all accounts, analyze journal entries and determine sub-populations for more focused and risk-based testing, and apply certain criteria to sub-populations to identify potential high-risk journal entries for further testing. — We did not identify any issues with completeness through our roll-forward procedures. We are satisfied with the results of our testing of specific relevant journal entries, which were identified for testing using the computer assisted auditing techniques.
Tangible capital assets	**WIP transfers to asset additions:** We utilized IDEA to ensure that asset additions to tangible capital assets recorded in the Citywide database transferred from work in progress are removed from work in progress completely. — We compared the asset additions listing to transfers out of work in progress and we investigated any significant asset additions that are not completely removed from work in progress. — We did not identify any issues with the completeness of transfers out of work in progress as any remaining items were supported. **Disposals:** We utilized IDEA to verify that assets that were disposed of during the year were completely removed from the register of assets in the Citywide database. — Our comparison of the disposals listing to the asset register continued to list assets that were disposed of, however, consistent with our findings in the past, they were identified with unique asset IDs and were all reported at nil cost values. — We did not identify any issues with the overstatement of assets being retained on the books for disposed assets. **Depreciation expense:** We utilized IDEA to analyze depreciation expense on an asset level. — We replicated the formula used to determine individual assets' annual amortization expense and recalculated an expected amount after verifying the appropriate inputs were used. We did not find any issues in our recalculation of amortization expense compared to the amounts recorded by the City.

Holdback completeness	We utilized D&A to evaluate whether construction holdbacks liabilities have been completely and consistently recorded for significant projects in work in progress at year-end. — We obtained the asset register for work in progress by project ID and the listing of contractor expenditures by business unit. We compared the holdbacks details from these two listings to identify significant projects that did not include a holdback. We did not find any issues with the completeness of holdbacks liabilities.
Cash deposits deferred revenue	We utilized D&A to evaluate the year-over-year change (on a project level) for 100% of the population of projects for which cash deposits have been collected in the current and prior year. – We used the cash deposits reconciliation listing for current year and prior year. We extracted cash receipts details from the prior year listing and compared them to cash on hand in the current year listing to determine if the deferred revenue roll-forward was complete and accurately calculated. There were no issues with the completeness of prior year deposits in the records of the current year.

Significant accounting policies and practices

Initial selections

There were no initial selections of significant accounting policies and practices. The following new accounting policy was effective and applied during the year as required under Public Sector Accounting Standards.

Changes

Changes to significant accounting policies and practices and the impact on the financial statements are disclosed in note 1(q) to the financial statements.

Beginning in fiscal 2019, the City is now required to adopt the following new public sector accounting standard (PSAS), which was applied prospectively:

PS 3430 – Restructuring Transactions

- This section establishes standards on how to account for and report restructuring transactions by both transferors and recipients of asset and/or liabilities, together with related program and operating responsibilities. Individual assets and liabilities received in a restructuring transaction should be recognized by the recipient if they meet the definitions of assets and liabilities and applicable recognition criteria at the restructuring date. Individual assets and liabilities transferred in a restructuring transaction should be derecognized by the transferor if they no longer meet the definition of assets and liabilities and applicable recognition criteria at the restructuring date.

- The City has internal policies to identify and monitor restructuring transactions. Our findings from our review of internal policies and procedures were consistent in this regard. At the completion of the audit, we will obtain from management a signed representation letter indicating that there were no restructuring transactions that were not identified to us or disclosed in the financial statements.

– As at December 31, 2019, and for the year then ended, the City does not have any restructuring transactions, as defined by the PS3430 to report.

Other matters

Professional standards require us to communicate to the Committee Other Matters, such as material inconsistencies or material misstatements between MD&A and the audited financial statements, identified fraud or non-compliance with laws and regulations, consultations with other accountants, significant matters relating to the Entity's related parties, significant difficulties encountered during the audit, and disagreements with management.

We have highlighted below other significant matters that we would like to bring to your attention:

Matter	Comments
Subsequent event **(note 17(a) to the financial statements)**	– In March 2020, the COVID-19 outbreak was declared a pandemic by the World Health Organization. This matter has far-reaching consequences for many organizations. – We have considered the potential impact on the financial statements with management and determined that a subsequent events disclosure is warranted. Financial implications are not fully known at this time. – We also updated our discussion with management on their assessment of the City as a going concern. Management notes that while there are closures of certain facilities and services and reduced revenues, management has asserted that its financial position is adequate to support the continued use of the going concern assumption at this time, and that there are cost savings from closures. – Disclosure describing the COVID-19 event and the potential financial implications of it to the City are included in the financial statements.

Uncorrected differences and Corrected Adjustments

Differences and adjustments include disclosure differences and adjustments.

Professional standards require that we request of management and the Committee that all identified differences be corrected. We have already made this request of management.

Uncorrected differences

We did not identify differences that remain uncorrected.

Corrected adjustments

We did not identify any adjustments that were communicated to management and subsequently corrected in the financial statements.

Control deficiencies

In accordance with professional standards, we are required to communicate to the Committee significant deficiencies in internal control over financial reporting (ICFR) that we identified during our audit.

The purpose of our audit is to express an opinion on the financial statements. Our audit included consideration of ICFR in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of ICFR. The matters being reported are limited to those deficiencies that we have identified during our audit and that we have concluded are of sufficient importance to merit being reported to the audit committee.

Significant deficiencies

There were no significant deficiencies identified.

Other observations

Item	Observation
Vacation accrual	– Disclosed in the financial statements is vacation entitlements liability (see note 5(c)), which is $7.6M in 2019 and $6.6M in 2018. The City's various collective agreements, Management bylaw and other HR policies permit certain maximum days to be carried over if unused. We note that there is an upward trend in this accrual over the past several years and we understand that this increase is due to factors such as compensation increases and increased number of unused days carried over. – We note that there are several risks associated with maintaining high levels of vacation accruals, for example, the cost of those vacation entitlements become increasingly more expensive as compensation levels increase, it can be potentially disruptive to the City's operations in the case where employees are granted extended leaves, and the financial impact to the City's financial position becomes less favourable as more reliance is placed on reserves or future funding in order to fund this liability. – In line with leading practices, we recommend that management carefully assess vacation entitlements, and put a plan in place to draw down on entitlements in order to better manage this liability and avoid servicing it at a higher cost than necessary. We note that in 2020, this liability is anticipated to amplify as employees defer vacation plans in light of COVID-19 and associated travel restrictions. We understand that senior management has issued formal communications to staff to encourage vacation usage. The City should consider developing and enforcing an effective policy with a specific objective of drawing down the liability. – Additionally, as another leading practice and as a fraud prevention measure, we note that management should ensure that staff take annual vacations and that another employee perform their work in their absence. This cost efficient control is one of the most effective methods of identifying any potential irregularities in performance. It also provides cross training for succession planning purposes.

Current developments and audit trends

Thought Leadership

Our discussions with you and what KPMG is seeing in the marketplace—both from an audit and industry perspective—indicate the following is specific information that will be of particular interest to you. We would, of course, be happy to further discuss this information with you at your convenience.

Thought Leadership	Overview	Links
Audit & Assurance Insights	Curated thought leadership, research and insights from subject matter experts across KPMG in Canada	Learn more
The business implications of coronavirus (COVID 19)	Resources to help you understand your exposure to COVID-19, and more importantly, position your business to be resilient in the face of this and the next global threat.	Learn more
	Financial reporting and audit considerations: The impact of COVID-19 on financial reporting and audit processes.	Learn more
	KPMG Global IFRS Institute - COVID-19 financial reporting resource center.	Learn more
Return to the Workplace	As all levels of government begin to take steps toward re-opening the country and restarting our economy, planning for the return to a physical workplace is quickly becoming a top priority for many organizations. With the guidelines for the pandemic continuing to evolve daily, there are many considerations, stages and factors employers need to assess in order to properly develop a robust action plan which can ensure the health and safety of their workforce. Questions for your leadership team: • Can your organization continue to operate remotely for the near future without any significant challenges? • If productivity levels have not been impacted, is the cost of real estate necessary for the organization? • What is the mental health risk to your employees from continuing to work remotely? • How many employees need to be in a physical office to properly perform their roles? • How many employees depend on public transit to get to your office(s)? • Do you have the capabilities to screen, track and isolate infected employees to prevent the spread of the virus within the confines of a physical workplace?	Learn more

How audit committees can respond to COVID-19	As the effects of the COVID-19 outbreak continue to evolve, organizations are racing to understand the business risks and implications on their financial reporting. The mandate of the audit committee includes critical items to be considered during the COVID-19 outbreak.	Learn more
Accelerate	Accelerate is a KPMG trends report and video series that includes the perspective of subject matter leaders from across KPMG in Canada on seven key issues impacting organizations today that are disrupting the audit committee mandate.	Learn more
Momentum	A quarterly Canadian newsletter which provides a snapshot of KPMG's latest thought leadership, audit and assurance insights and information on upcoming and past audit events – keeping management and board members abreast on current issues and emerging challenges within audit.	Sign-up now
Current Developments	Series of quarterly publications for Canadian businesses including Spotlight on IFRS, Canadian Securities & Auditing Matters and US.	Learn more
Board Leadership Centre	Leading insights to help board members maximize boardroom opportunities.	Learn more
2019 Audit Quality and Transparency Report	Learn about KPMG's ongoing commitment to continuous audit quality improvement. We are investing in new innovative technologies and building strategic alliances with leading technology companies that will have a transformative impact on the auditing process and profession. How do we seek to make an impact on society through the work that we do?	Learn more
Put your data to work to gain competitive advantage	There is no "digital economy". The economy is digital and "digits" refer to data. Data is the lifeblood of every organization on this planet and organizations that embrace this notion are well positioned to grow as industries continue to evolve and disrupt at an ever increasing pace.	Learn more
Predictive analytics, it works	CEOs recognize the value that predictive analytics delivers to their decision-making process.	Learn more
Creating the workforce of the future	You can't transform the organization without also transforming the workforce. It may be time to rethink the people strategy.	Learn more
Bracing for digital disruption	The digital revolution may be well into its prime, but the disruption is far from over. New and emerging technologies continue to shape (and reshape) how organizations operate and adapt to their customers. While these tools have opened the doors to new capabilities and market opportunities, they have also driven the need for stronger and more adaptive risk management strategies.	Learn more

Public Sector Accounting Standards

Title	Details	Link
Public Sector Update – connection series	Public Sector Accounting Standards are evolving – Get a comprehensive update on the latest developments from our PSAB professionals. Learn about current changes to the standards, active projects and exposure drafts, and other items.	Contact your KPMG team representative to sign up for these webinars. Public Sector Minute Link

The following are upcoming changes that are effective in the current year or will be effective in future periods as they pertain to Public Sector Accounting Standards. We have provided an overview of what these standards are and what they mean to your financial reporting so that you may evaluate any impact to your future financial statements.

Standard	Summary and implications
Asset Retirement Obligations (applicable for the year ending December 31, 2023 with option for retrospective application effective December 31, 2022)	– A new standard, PS3280 *Asset Retirement Obligations*, has been approved that is effective for fiscal years beginning on or after April 1, 2022 (the City's 2023 year-end). – The new standard addresses the recognition, measurement, presentation and disclosure of legal obligations associated with retirement of tangible capital assets in productive use. Retirement costs would be recognized as an integral cost of owning and operating tangible capital assets. PSAB currently contains no specific guidance in this area. – The ARO standard would require the public sector entity to record a liability related to future costs of any legal obligations to be incurred upon retirement of any controlled tangible capital assets ("TCA"). The amount of the initial liability would be added to the historical cost of the asset and amortized over its useful life. – As a result of the new standard, the public sector entity would have to: o consider how the additional liability will impact net debt, as a new liability will be recognized with no corresponding increase in a financial asset; o carefully review legal agreements, senior government directives and legislation in relation to all controlled TCA to determine if any legal obligations exist with respect to asset retirements; o begin considering the potential effects on the organization as soon as possible to coordinate with resources outside the finance department to identify AROs and obtain information to estimate the value of potential AROs to avoid unexpected issues.

Standard	Summary and implications
Revenue	– A new standard, PS3400 *Revenues*, has been approved that is effective for fiscal years beginning on or after April 1, 2023 (the City's 2024 year-end). – The new standard establishes a single framework to categorize revenues to enhance the consistency of revenue recognition and its measurement. – The standard notes that in the case of revenues arising from an exchange, a public sector entity must ensure the recognition of revenue aligns with the satisfaction of related performance obligations. – The standard notes that unilateral revenues arise when no performance obligations are present, and recognition occurs when there is authority to record the revenue and an event has happened that gives the public sector entity the right to the revenue.
Financial Instruments and Foreign Currency Translation	– New accounting standards, PS3450 *Financial Instruments*, PS2601 *Foreign Currency Translation*, PS1201 *Financial Statement Presentation* and PS3041 *Portfolio Investments* have been approved by PSAB and are effective for years commencing on or after April 1, 2022 (the City's 2023 year-end). – Equity instruments quoted in an active market and free-standing derivatives are to be carried at fair value. All other financial instruments, including bonds, can be carried at cost or fair value depending on the government's choice and this choice must be made on initial recognition of the financial instrument and is irrevocable. – Hedge accounting is not permitted. – A new statement, the Statement of Re-measurement Gains and Losses, will be included in the financial statements. Unrealized gains and losses incurred on fair value accounted financial instruments will be presented in this statement. Realized gains and losses will continue to be presented in the statement of operations. – Based on stakeholder feedback received, PSAB is considering certain scope amendments to PS 3450 *Financial Instruments*. An exposure draft with the amendments is expected to be issued in 2020. The proposed amendments are expected to include the accounting treatment of bond repurchases, scope exclusions for certain activities by the federal government, and improvements to the transitional provisions.
Employee Future Benefit Obligation	– PSAB has initiated a review of sections PS3250 *Retirement Benefits* and PS3255 *Post-Employment Benefits, Compensated Absences and Termination Benefits*. Given the complexity of issues involved and potential implications of any changes that may arise from this review, the project will be undertaken in phases. Phase I will address specific issues related to measurement of employment benefits. Phase II will address accounting for plans with risk sharing features, multi-employer defined benefit plans and sick leave benefits. – Three Invitations to Comment were issued and have closed. The first Invitation to Comment sought guidance on whether the deferral provisions in existing public sector standards remain appropriate and justified and the appropriateness of accounting for various components of changes in the value of the accrued benefit obligation and plan assets. The second Invitation to Comment sought guidance on the present value measurement of accrued benefit obligations. A third Invitation to Comment sought guidance on non-traditional pension plans. – The ultimate objective of this project is to issue a new employment benefits section to replace existing guidance.

Standard	Summary and implications
Public Private Partnerships ("P3")	– A taskforce was established in 2016 as a result of increasing use of public private partnerships for the delivery of services and provision of assets. The objective is to develop a public sector accounting standard specific to pubic private partnerships. – A Statement of Principles ("SOP") was issued in August 2017 which proposes new requirements for recognizing, measuring and classifying infrastructure procured through a public private partnership. An Exposure Draft of the new standard was issued in November 2019. – Public private partnership infrastructure is recognized as an asset when the public sector entity acquires control of the infrastructure. A liability is recognized when the asset is recognized and may be a financial liability, a performance obligation or a combination of both. – An infrastructure asset acquired in an exchange transaction is recorded at cost which is equal to its fair value on the measurement date. The liability is measured at the cost of the infrastructure asset initially. – Subsequently, the infrastructure asset is amortized in a rational and systematic manner over its useful life. – Subsequent measurement of the financial liability would reflect the payments made by the public sector entity to settle the liability as well as the finance charge passed on to the public sector entity through the public private partnership agreement. – Subsequent measurement of the performance obligation: revenues are recognized and the liability reduced in accordance with the substance of the public private partnership agreement.
Concepts Underlying Financial Performance	– PSAB is in the process of reviewing the conceptual framework that provides the core concepts and objectives underlying Canadian public sector accounting standards. – PSAB is developing two exposure drafts (one for a revised conceptual framework and one for a revised reporting model) with two accompanying basis for conclusions documents and resulting consequential amendments. PSAB expects to issue the two exposure drafts and accompanying documents in 2020. – A Statement of Concepts ("SOC") and Statement of Principles ("SOP") were issued for comment in May 2018. – The SOC proposes a revised, ten chapter conceptual framework intended to replace PS 1000 *Financial Statement Concepts* and PS 1100 *Financial Statement Objectives*. The revised conceptual framework would be defined and elaborate on the characteristics of public sector entities and their financial reporting objectives. Additional information would be provided about financial statement objectives, qualitative characteristics and elements. General recognition and measurement criteria, and presentation concepts would be introduced. – The SOP includes principles intended to replace PS 1201 *Financial Statement Presentation*. The SOP proposes: o Removal of the net debt indicator, except for on the statement of net debt where it would be calculated exclusive of financial assets and liabilities that are externally restricted and/or not available to settle the liabilities or financial assets. o Changes to common terminology used in the financial statements, including re-naming accumulated surplus (deficit) to net assets (liabilities). o Restructuring the statement of financial position to present non-financial assets before liabilities. o Removal of the statement of remeasurement gains (losses) with the information instead included on a new statement called the statement of changes in net assets (liabilities). This new statement would present the changes in each component of net assets (liabilities). o A new provision whereby an entity can use an amended budget in certain circumstances. – Inclusion of disclosures related to risks and uncertainties that could affect the entity's financial position.

Standard	Summary and implications
2019 – 2020 Annual Improvements	– PSAB adopted an annual improvements process to make minor improvements to the CPA Canada Public Sector Accounting (PSA) Handbook or Statements of Recommended Practices (other guidance). – The annual improvement process: o clarifies standards or other guidance; or o corrects relatively minor unintended consequences, conflicts or oversights. – Major or narrow scope amendments to the standards or other guidance are not included in the annual improvement process.
International Strategy	– PSAB is in the process of reviewing its current approach towards International Public Sector Accounting Standards (IPSAS). This project may result in changes to the role PSAB plays in setting standards in Canada. – A consultation paper was released for comment in May 2018 and has closed. The consultation paper described the decision-making criteria PSAB expects to consider in evaluating the international strategy that best serves the public sector. It also introduced four proposed international strategies that PSAB considers to be viable. Over 2017-2021 period, PSAB intends to do the following: o conduct research on differences between Canadian Public Sector Accounting Standards and International Accounting Standards; o learn about experiences of other jurisdictions that choose to follow IPSAS; publish a consultation paper to get the opinion of stakeholders; o and, develop options for PSAB's International strategy.
Purchased Intangibles	– As a result of stakeholder feedback received, PSAB will revisit validity of the prohibition against recognizing purchased intangibles in public sector financial statements and will consider a narrow scope amendment. – Input received in response to the 2018 conceptual framework and reporting model documents for comment supported PSAB relocating the recognition prohibitions from the conceptual framework to the standards level. This is a bigger issued for Indigenous governments. PSAB is looking into the question of why purchased intangibles acquired through an exchange transaction cannot be recognized in public sector financial statements as they are measureable at the price in the transaction.

New auditing standards that are effective for fiscal year 2020 are as follows:

Standard	Expected impact on the audit	Reference
CAS 540, Auditing Accounting Estimates and Related Disclosures **Effective for audits of Entities with year-ends on or after December 15, 2020**	— more emphasis on the need for exercising professional skepticism — more granular risk assessment to address each of the components in an estimate (method, data, assumptions) — more granular audit response designed to specifically address each of the components in an estimate (method, data, assumptions) — more focus on how we respond to levels of estimation uncertainty — more emphasis on auditing disclosures related to accounting estimates — more detailed written representations required from management	CPA Canada Client Briefing

Appendices

Content

Appendix 1: Other Required Communications

In accordance with professional standards, there are a number of communications that are required during the course of and upon completion of our audit. These include:

Engagement letter

The objectives of the audit, our responsibilities in carrying out our audit, as well as management's responsibilities, are set out in the engagement letter dated November 30, 2018 as provided by management.

Audit findings report

This report.

Auditors' report

The conclusion of our audit is set out in our draft auditors' report attached to the draft financial statements.

Management representation letter

In accordance with professional standards, a copy of the management representation letter is provided to the Committee by Management.

Independence

We are independent and have extensive quality control and conflict checking processes in place. We provide complete transparency on all services and follow Committee and Council approved protocols.

Audit quality

Audit Quality (AQ) is at the core of everything we do at KPMG. Appendix 2 provides more information on AQ.

The following links are external audit quality reports for referral by the audit committee:

- CPAB Audit Quality Insights Report: 2019 Annual Inspections Results
- CPAB Audit Quality Insights Report: 2019 Fall Inspection Results

Required inquiries

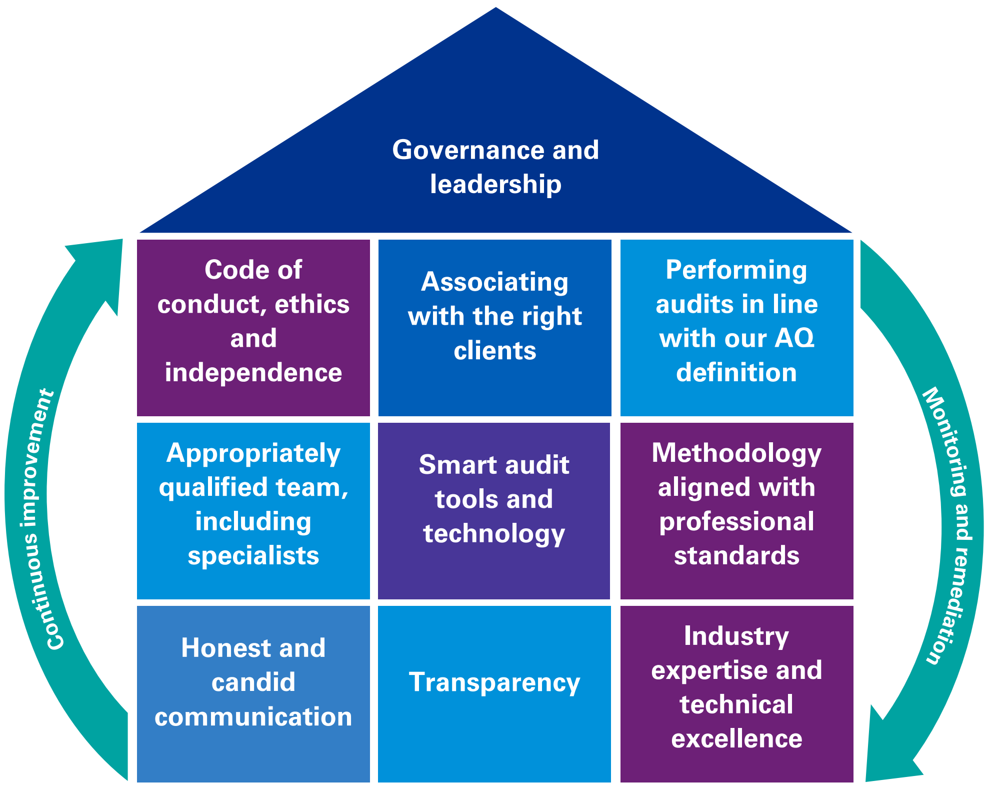
Professional standards require that we obtain your views on risk of fraud and other matters. We make similar inquiries of management.

- What are your views about fraud risk at the entity?
- How do those charged with governance exercise effective oversight of management's processes for identifying and responding to the risk of fraud in the entity and internal controls management has established to mitigate these fraud risks?
- Are you aware of or have you identified any instances of actual, suspected, or alleged fraud, including misconduct or unethical behaviour related to financial reporting or misappropriation of assets? If so, have the instances been appropriately addressed and how have they been addressed?
- Is the entity in compliance with laws and regulations?
- Has the entity entered into any significant usual transactions?

Appendix 2: Audit Quality and Risk Management

KPMG maintains a system of quality control designed to reflect our drive and determination to deliver independent, unbiased advice and opinions, and also meet the requirements of Canadian professional standards.

Quality control is fundamental to our business and is the responsibility of every partner and employee. The following diagram summarizes the key elements of our quality control system.



Audit Quality Framework

What do we mean by audit quality?

Audit Quality (AQ) is at the core of everything we do at KPMG.

We believe that it is not just about reaching the right opinion, but how we reach that opinion.

We define 'audit quality' as being the outcome when audits are:

- Executed consistently, in line with the requirements and intent of applicable professional standards within a strong system of quality controls and
- All of our related activities are undertaken in an environment of the utmost level of **objectivity, independence, ethics,** and **integrity**.

Our AQ Framework summarises how we deliver AQ. Visit our Audit Quality Resources page for more information including access to our Audit Quality and Transparency report.

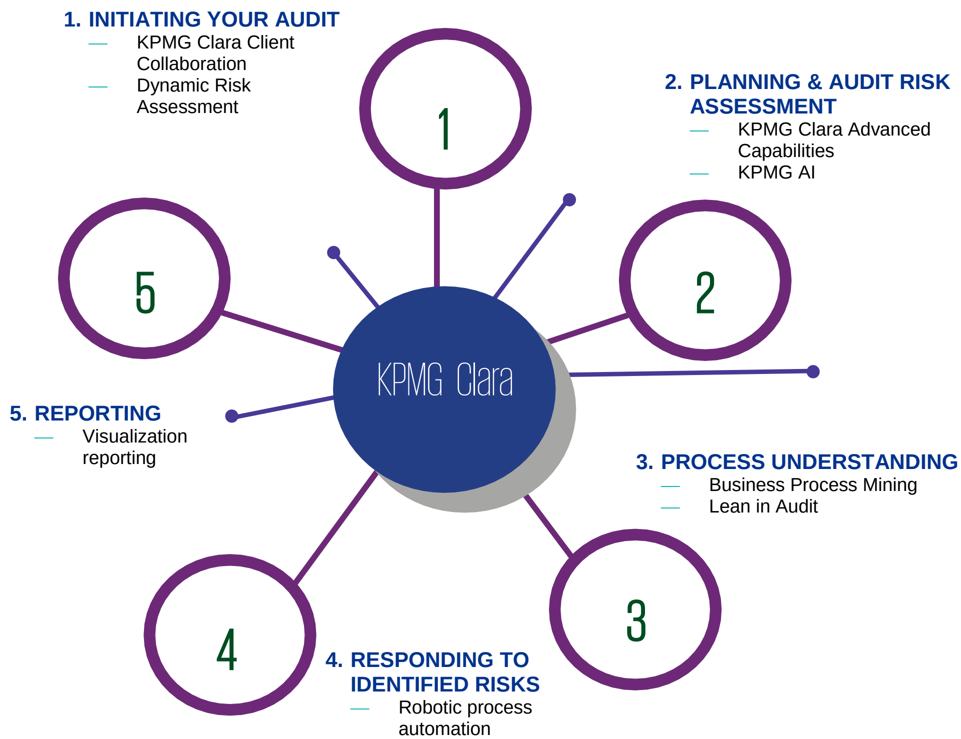
Appendix 3: Use of technology in the audit

Clara is KPMG's integrated, smart global audit platform that allows our teams globally to work simultaneously on audit documentation while sharing real time information. Clara also leverages advanced technology in the execution of various audit procedures, for overall risk assessment and for performing substantive audit procedures over 100% of selected transactions through the use of robotic process automation (KPMG "Bots"). KPMG's use of technology provides for:

1. a **higher quality audit** – looking at 100% of selected data
2. a **more efficient audit** as we are focussed on the transactions that are considered higher risk and
3. an audit that provides **insights into your business** through the use of technology in your audit with our extensive industry knowledge.

We are also actively piloting Artificial Intelligence ("AI") tools which will be used in future audits.

Our five-phased audit approach



Appendix 4: KPMG's audit approach and methodology

Collaboration in the audit
A dedicated KPMG Audit home page gives you real-time access to information, insights and alerts from your engagement team.

Issue identification
Continuous updates on audit progress, risks and findings before issues become events.

Data-driven risk assessment
Automated identification of transactions with unexpected or unusual account combinations – helping focus on higher risk transactions and outliers.

Deep industry insights
Bringing intelligence and clarity to complex issues, regulations and standards.

Analysis of complete populations
Powerful analysis to quickly screen, sort and filter 100% of your journal entries based on high-risk attributes.

Reporting
Interactive reporting of unusual patterns and trends with the ability to drill down to individual transactions.

KPMG

Appendix 5:

Preparingfor PSAB Standard Changes

Are you ready to implement PSAB's impactful series of new standards?

Public sector entities are preparing to implement three significant Public Sector Accounting standards through 2023. These standards will impact not only your accounting policies, but also how Finance engages key stakeholders.

Asset Retirement Obligations

PS3280 addresses the reporting of legal obligations associated with the retirement of certain tangible capital assets and solid waste landfill sites by public sector entities.**PS3280 will apply to fiscal years beginning on or after April 1, 2022 (the City's 2023 fiscal year). Earlier adoption is permitted. Three transition options are available – retroactive, modified retroactive, prospective.**

Asset retirement activities are defined to include all activities related to an asset retirement obligation. These may include but are not limited to:

- decommissioning or dismantling a tangible capital asset that was acquired, constructed or developed
- decontamination created by the normal use of the tangible capital asset
- post-retirement activities such as monitoring
- constructing other tangible capital assets in order to perform postretirement activities

With the introduction of PS3280 PSAB has withdrawn existing Section PS3270, solid waste landfill closure and post-closure liability.

Some examples of asset retirement obligations which fall under scope of proposed PS3280 include:

- end of lease provisions (from a lessee perspective)
- removal of radiologically contaminated medical equipment
- closure and post-closure obligations associated with landfills
- wastewater or sewage treatment facilities
- septic beds
- firewater holding tanks
- fuel storage tank removal

Under PS3280, an asset retirement obligation should be recognized when, as at the financial reporting date, ALL of the following criteria are met:

- there is a legal obligation to incur retirement costs in relation to a tangible capital asset
- it is expected that future economic benefits will be given up
- the past transaction or event giving rise to the liability has occurred
- a reasonable estimate of the amount can be made

This accounting standard will have implications for your organization if you report under the Public Sector Accounting Standards.

Are You Ready?

1. *Has a project plan been developed for the implementation of this section?*
2. *Has Finance communicated with key stakeholders, including Council or Board on the impact of this section?*
3. *Does Finance communicate with representatives of the Public Works, Asset Management, Facilities Management or Legal functions through the financial reporting process?*
4. *Has a complete inventory been developed of all inactive or active assets or sites, to provide a baseline for scoping of potential retirement obligations?*
5. *If a complete inventory has been developed, does it reconcile back to information currently reported in the entity's financial statements for tangible capital assets or contaminated sites?*
6. *Does your entity have data on non-recorded assets or sites (ie: assets which were originally expensed on purchase, or recorded at no book value) which could have retirement obligations?*
7. *Does your entity have an active solid waste landfill site?*
8. *If yes, does your entity have an existing estimate of the full costs to retire and monitor the landfill site?*
9. *Is your entity aware of any of its buildings which have asbestos?*
10. *If so, does your entity have information to inform a cost estimate to remove/ treat the asbestos?*
11. *Is your entity aware of underground fuel storage tanks or boilers which must be removed at end of life?*
12. *If so, does your entity have information to inform a cost estimate to remove the tanks?*
13. *Is your entity aware of any lease arrangements where it will be required to incur costs to return the premises to pre-existing conditions at the end of the lease?*
14. *Has your entity determined if it has any sewage or wastewater treatment plants which have closure plans or environmental approvals which require full or partial retirement of the plant at the end of its life?*
15. *Is your entity aware of any other contractual or legal obligations to retire or otherwise dismantle or remove an asset at the end of its life?*

Revenues

PS3400 outlines a framework describing two categories of revenue – transactions with performance obligations (exchange transactions) and transactions without performance obligations (unilateral transactions).

- This section will apply to fiscal years beginning on or after April 1, 2023, with earlier adoption permitted.
- This Section may be applied retroactively or prospectively.
- This section will not impact the present accounting for taxation revenues and government transfers.

Transactions which give rise to one or more performance obligations are considered to be exchange transactions. Performance obligations are defined as enforceable promises to provide goods or services to a payer as a result of exchange transactions. Revenue from an exchange transaction would be recognized when the public sector entity has satisfied the performance obligation(s), at a point in time or over a period of time.

If no performance obligations are present, the transaction would represent unilateral revenue, and be recognized when the public sector entity has the authority to claim or retain an inflow of economic resources and a past event gives rise to a claim of economic resources.

Public sector entities will need to review their revenue recognition policies for in-scope transaction types. Impacted areas may include:

- Development charges
- Permits
- Licences
- Advertising programs

Are You Ready?

1. *Has the entity identified any revenue-generating transactions other than taxation or government transfer revenues which create performance obligations (ie: the entity is required to provide a good or service to earn that revenue)?*
2. *If so, has the entity reviewed its accounting policies for these transactions to verify revenue is recognized only as performance obligations are being met?*
3. *Has the entity quantified the impact of any change in accounting policy, or determined that there is no impact?*

Financial Instruments

PS3450 establishes standards on how to account for and report all types of financial instruments including derivatives.

- This Section applies to fiscal years beginning on or after April 1, 2022. Earlier adoption is permitted.
- Government organizations that applied the CPA Canada Handbook – Accounting prior to their adoption of the CPA Canada Public Sector Accounting Handbook applied this Section to fiscal years beginning on or after April 1, 2012.
- This section must be adopted with Section PS 2601, Foreign Currency Translation.
- Specific transition requirements are outlined in the section.

This section prescribes a fair value measurement framework for derivatives, and equity instruments that are quoted in an active market.

Where an entity manages risks, the investment strategy, or performance of a group of financial assets, financial liabilities or both on a fair value basis, they may also be meased at fair value.

Other financial instruments are measured at cost/ amortized cost.

Changes in the fair value of a financial instrument in the fair value category are recognized in the Statement of Remeasurement Gains and Losses as a remeasurement gain or loss until the financial instrument is derecognized.

- Upon derecognition, the remeasurement gain or loss is realized in the Statement of Operations.

Are You Ready?

1. *Does the entity hold any financial assets which are equity or derivative instruments?*
2. *Has the entity determined if it has any embedded derivatives that might arise from existing contractual arrangements?*
3. *Does the entity have other financial assets which it assesses performance of based on fair value, and for which it might elect a fair value measure?*
4. *If yes to any of the above three questions, does the entity have readily observable market data to inform a fair value measure?*
5. *Has the entity reviewed existing financial instrument note disclosure in the financial statements to determine any required revisions to meet the requirements of this section?*
6. *Does the entity enter into transactions involving foreign exchange?*
7. *Does the entity hold any monetary assets and monetary liabilities, or non-monetary assets denominated in a foreign currency?*

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