

Staff Report



To	City Council
Service Area	Corporate Services
Date	Monday, July 20, 2020
Subject	2019 Consolidated Financial Statements and External Audit Findings Report

Recommendation

That the City of Guelph 2019 Consolidated Financial Statements and External Audit Findings Report, dated July 20, 2020, be approved.

Executive Summary

Purpose of Report

To present and provide an overview of the City's 2019 Consolidated Financial Statements, including related entities' Financial Statements; and to provide Council with the City's external audit results as reported in KPMG LLP's 2019 Audit Findings Report.

Key Findings

KPMG LLP, the City's external auditor, performed an audit of the City's 2019 Consolidated Financial Statements in accordance with generally accepted auditing standards and expressed an unqualified or clean opinion that the statements present fairly, in all material respects, the financial position of the City. There were no concerns raised in KPMG LLP's External Audit Findings Report included as Attachment-5 to this report.

The City's 2019 consolidated net financial assets increased by \$48.2 million over 2018, a continued affirmation of financial health and stability of the corporation. The key 2019 financial indicators are presented in the Corporate Financial Performance Measures Dashboard on the City's website, and include:

- Cash and investment holdings increase of \$80.2 million over December 31, 2018, and a ratio of 1.20:1 in comparison with total reserves and reserve funds (including deferred contributions). This is an increase from the 2018 consolidated cash and investments to reserves and reserve funds ratio of 1.17.
- The City has continued to maintain a low tax receivable position as a percentage of total taxes levied; the City is at 1.98% compared to the Ontario southwest regional average of 5.4% for 2018 (the 2019 data is not yet available).
- The City repaid \$13.9 million in debt principle and incurred \$3.2 million of interest on long-term debt. The City continues to have strong debt ratios, including debt to total reserves, debt outstanding per \$100,000 of

unweighted assessment, and debt interest as a percentage of own source revenue. The City issued debt in 2019 totaling \$33.1 million at an average rate of 2.43% interest.

- The balance in the City's reserves and reserve funds totals \$250.6 million, an increase of \$33.0 million over the balances at December 31, 2018.

The City is required to consolidate and report on related entities as a requirement of Public Sector Accounting Standards (PSAS). The entities, and highlights of their 2019 Audited Financial Statements include:

- The Elliott Community (The Elliott) reported a 2019 excess of revenues over expenses of \$1.2 million compared to \$1.1 million in 2018. The net deficit of \$5.8 million at the beginning of the year was reduced to \$4.6 million by the end of the year. Operating revenue increased by approximately \$300 thousand and operating expenses increased by approximately \$450 thousand, however bequests totaling \$290 thousand were received during the year offsetting what would have otherwise been a decrease in the annual surplus.
- The Downtown Guelph Business Association (DGBA) reported a 2019 excess of revenues over expenses of \$8 thousand compared to \$51 thousand in 2018. In 2019, net assessment write-offs were \$13 thousand, whereas recoveries of \$4 thousand were reported on the same line in 2018. Special projects contributions also increased by \$22 thousand in 2019.
- Wellington-Dufferin-Guelph Public Health (Public Health) reported an excess of revenue over expenditures of \$805 thousand (2018 - \$325 thousand). The City proportionately consolidates the health unit based on the percentage of municipal funding contributed which was unchanged from 2018 at 46.3%. This percentage is based on the 2016 census population.
- Guelph Municipal Holdings Inc. (GMHI) and Guelph Junction Railway Limited (GJR) both have a formal process for reporting their Financial Statements to Council in accordance with each entity's Shareholder Declaration; for this reason their Financial Statements have not been included as attachments.
- A variance analysis of the Guelph Police Service Board (Police Board) and Guelph Public Library Board (Library Board) was included in report 2020-41 2019 Year-end Operating Variance Report and Surplus Allocation.

Financial Implications

An unqualified opinion of the 2019 Consolidated Financial Statements will assist the City in obtaining a fair credit rating which has the potential to lower its borrowing costs as well as support grant-funding requests from outside organizations.

The City's net financial position is a key indicator of its overall fiscal condition and is used in the City's annual credit rating review. A stable financial position helps ensure the City of Guelph meets service levels and infrastructure standards without resorting to excessive rate increase or disruptive cuts in service.

Report

City Council annually reviews and approves the City of Guelph's audited Consolidated Financial Statements as required under the Municipal Act, 2001.

Review and approval of the audited 2019 Consolidated Financial Statements and review of KPMG LLP's Audit Findings Report satisfy the following Audit Committee responsibilities:

- Understand the scope of the external auditor's review of internal financial control over financial reporting and obtain reports on significant findings and recommendations, together with management's responses and the timing of the disposition of significant findings;
- After consultation with the Treasurer and the external auditors, gain reasonable assurance, at least annually, of the quality and sufficiency of the City's accounting, financial personnel and other resources;
- Review with staff and the external auditors the results of the audit, including any difficulties encountered, and all other matters required to be communicated to the Committee under generally accepted auditing standards;
- If required, at the conclusion of the audit, consult with the external auditors, without the presence of staff, about internal financial controls, compliance, and the completeness and accuracy of the City's Consolidated Financial Statements;
- Ensure the timely presentation of the external auditor's annual audit report to Council;
- Review significant accounting and reporting issues in terms of their impact on the Financial Statements, including complex or unusual transactions, areas high in subjectivity, and recent professional and regulatory pronouncements;
- Review the representation letter provided by staff to the external auditors;
- Prior to the presentation of the annual Financial Statements to Council, review the Financial Statements and consider whether they are complete, consistent with information known to Committee members, and reflect appropriate accounting principles; and
- Recommend to Council the approval and distribution of the annual consolidated Financial Statements.

Overview of the Consolidated Financial Statements

Please refer to Attachment-1 for the Draft Consolidated Financial Statements. These statements are required to be approved by Council in accordance with the Municipal Act, 2001.

The Consolidated Financial Statements have been prepared in accordance with PSAS, which require the consolidation of the following entities into the City's statements:

- The Elliott – fully consolidated
- DGBA – fully consolidated
- Public Health – proportionately consolidated (46.3%)
- GMHI – modified equity basis
- GJR – modified equity basis
- Police Board – fully consolidated
- Library Board – fully consolidated

Fully consolidated means that the full financial statements of those entities have been combined into the City's statements.

Proportionately consolidated means that only the City's share (46.3%) of Public Health's financial statements have been included in the City's statements. All inter-

organizational transactions have been eliminated between the City and the fully consolidated and proportionately consolidated entities.

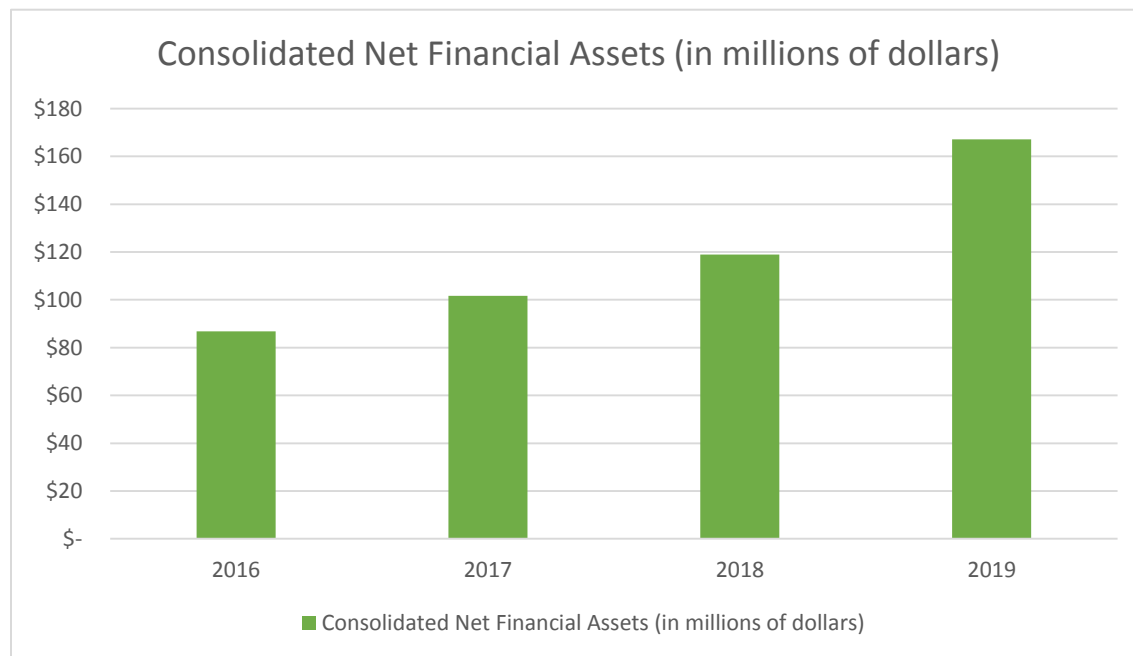
Modified equity basis means that the carrying value of the net assets of the investee are shown on the face of the City's Statement of Financial Position as an investment, and any gain or loss in carrying value is shown on the Statement of Operations as government business enterprises earnings. There are no inter-organizational transaction eliminations.

Statement of Financial Position

The Statement of Financial Position is a summary of the consolidated assets, liabilities and accumulated surplus, which includes reserves and reserve funds. The City's net financial position (net financial assets) is a key indicator of its overall fiscal health and is used by the credit rating agency in the City's annual rating review. As of December 31, 2019 the City's consolidated net financial assets totaled \$167.2 million, an increase of \$48.2 million from 2018. This continues a trend now spanning four years and indicates that the City and its consolidated entities are generating revenue to increase financial assets (increase of \$100.8 million in 2019) at a greater rate than the increase in financial liabilities (increase of \$52.5 million in 2019).

On a per capita basis, the City has also been trending upward with 2019 net financial assets per person of \$1,185, which is above the 2018 municipal average of \$517 and median of \$659 for single and lower tier municipalities. 2019 data is not yet available for comparison.

Figure 1 – Consolidated Net Financial Assets Trend (in millions)



Highlights

Total cash and investment holdings increased by \$80.2 million in 2019. Cash increased by \$4.7 million, the result of positive cash flows from operations of \$102.2 million and financing activities of \$46.2 million, and offset by \$143.7 million in negative cash flows from capital and investing activities. Net investment

acquisitions totaled \$75.4 million. The City meets the minimum target measure of cash and investment holdings which is a 1:1 ratio with the City's reserve and reserve fund balances including the deferred contributions on the Statement of Financial Position.

Accounts receivable

Accounts receivable increased by \$4.9 million in 2019 compared with the balance as at December 31, 2018. The two main contributors to this increase were HST receivable (increase of \$1.9 million) and amounts receivable from Alectra Utilities Corp. (Alectra) for water and wastewater revenues (\$3.0 million).

Loans and notes receivable

Loans and notes receivable decreased by \$2.5 million, mainly due to the funds remaining from the 2018 special dividend paid by Guelph Hydro Electric Systems Inc. (GHESI) to GMHI during the merger with Alectra being transferred to City investment accounts.

Investment in GJR

The City's investment in GJR increased by \$1.0 million as GJR had net income of just under \$1.1 million in 2019 and paid the City a dividend of \$80 thousand.

Investment in GMHI

The City's investment in GMHI increased by \$17.3 million mainly due to GMHI's investment in its electricity utility being brought up to market value through the accounting transactions required to report on the merger of GHESI and Alectra.

Deferred revenue

Developer agreement deferred revenue increased by \$700 thousand and other deferred revenue increased by \$2.3 million. The increase in other deferred revenue was driven by an increase in site plan security deposits totaling \$2.2 million, and deposits received in advance of work being completed for site servicing of \$584 thousand, and tree planting of \$277 thousand, as well as River Run ticket sales totaling \$200 thousand. These increases were offset by a decrease in building permit deferred revenue totaling \$1.0 million.

Deferred contributions

Deferred contributions include development charges (for growth-related capital expenditures), federal and provincial gas tax funds and parkland dedication and Ontario Building Code Act funds that have been received but not yet spent. In 2019 the City received \$59.5 million in deferred contributions and spent \$33.6 million on projects funded through these revenues, for a net increase of \$25.9 million to the year-end balance. The largest portion of this net increase was an increase of \$16.6 million in deferred development charges. Federal and provincial gas tax deferred contributions increased by \$5.6 million, and parkland dedication and Ontario Building Code deferred revenue increased by \$3.7 million.

Employee future benefits

Employee future benefits increased by \$4.5 million with an increase to the future liability for Workplace Safety and Insurance Board (WSIB) liability accounting for \$2.6 million of the increase, in addition to an increase of \$1.6 million for post-retirement benefits. The City is a Schedule II employer for WSIB (self-insured). The

liability reported on the City's balance sheet includes the present value of the projected future WSIB payments, including administration and other costs for past WSIB claims, plus the unamortized gains and losses which have occurred at past valuation dates. Gains and losses are amortized over the average remaining period for paying the WSIB benefits. The WSIB liability increase is mostly driven by WSIB claim volume and increased payments per claim. The post-retirement benefits liability increase is driven by changes to the Fire and Police retirement benefits.

Debt

The City issued debt in 2019 totaling \$33.1 million for several capital projects under By-law 20417, and The Elliott borrowed \$1.4 million on a line of credit. The City and its consolidated entities made debt principal repayments totaling \$13.9 million, for a net increase in debt principal outstanding of \$20.5 million at the end of 2019.

Other long-term liabilities

Other long-term liabilities include Tax Increment Based Grant (TIBG) liabilities for Heritage Redevelopment, Downtown Community Improvement Plan, and the Brownfield Redevelopment Community Improvement Plan. The liability for the Downtown Development TIBG decreased by \$2.5 million, while the liability for the Brownfield Redevelopment TIBG increased by \$1.8 million, for an overall net decrease of \$700 thousand in the liability.

Liability for contaminated sites

The liability for contaminated sites decreased by \$1 million as expenditures for contaminated sites remediation totaled \$1.1 million in 2019 and the present value of the remaining expenditures was adjusted for inflation.

Tangible capital assets

The City spent \$88.8 million to acquire tangible capital assets in 2019, with a further \$4.6 million being received in contributed subdivision assets for total tangible capital asset additions of \$93.4 million.

Statement of Operations and Accumulated Surplus

The City ended the year with an excess of revenues over expenditures of \$84.8 million (compared with \$55.6 million in 2018).

The audited Consolidated Financial Statements are prepared in accordance with PSAS, and as a result, the net surplus reported in these financial statements is different from the surplus reported by staff in the 2019 Year-end Operating Variance Report and Surplus Allocation Report (report 2020-41). Both numbers are computed using the same underlying data, however, as shown in Figure 2 they are presented differently based on the requirements of cash basis operating and capital budgeting versus accrual-based financial reporting.

Figure 2 – Reconciliation of PSAS surplus versus operating budget surplus

Description	Amount
Ending surplus - PSAS	\$84,807
Net capital-related revenues and depreciation	31,206

Description	Amount
Debt-related and non-cash items	(29,201)
Reserve related transfers	(75,527)
Consolidated entities	(1,757)
Total	\$9,528
Ending surplus – tax supported	\$5,478
Ending surplus – non-tax supported	4,050
Total	\$9,528
Difference	\$0

Revenue Highlights

Tax revenue is the largest source of income for the City, followed by user charges and contribution revenues. Total revenues increased by \$42.7 million in 2019 to \$527.2 million, largely due to government business enterprises earnings, property taxes, provincial government contributions, and user charges.

Tax revenue

Tax revenue increased by \$11.0 million in 2019 overall predominantly due to the general levy increasing by \$9.9 million as a result of Council's approved tax levy increase. Also of note, the supplementary levy decreased by \$300 thousand from 2018 and penalties and interest increased by \$100 thousand.

User charges

User charges increased by \$2.4 million, driven largely by increases in fare bus passes, wastewater, storm water, and water consumption charges.

Contributions

Contribution revenues are received from the federal and provincial governments, other municipalities, and developers. The increase in year-over-year contribution revenues totaled \$5.5 million and was driven by an increase to provincial contributions, half of which was an increase to provincial child care funding provided to the County of Wellington (the City records its share of provincial social services funding as revenue). A large portion of contribution revenue is directly related to capital spending and therefore can fluctuate year-to-year with large projects funded by grants and development charges.

Investment income

Investment income increased by \$1.9 million largely due to the increased reserve and reserve fund balances and the average rate of return increasing from 2.19% in 2018 to 2.45% in 2019.

Recoveries

Recoveries increased by \$1.3 million, with \$600 thousand of this increase being other revenue from The Elliott consolidation.

Loss on disposal of tangible capital assets

The most significant asset disposals in 2019 were the police headquarters which is nearing completion of a complete renewal of the existing building, sale of vehicles and equipment that reach the end of life, and sale of industrial land at the Hanlon Creek Business Park. In total, these transactions generated a loss of \$1.4 million in 2019.

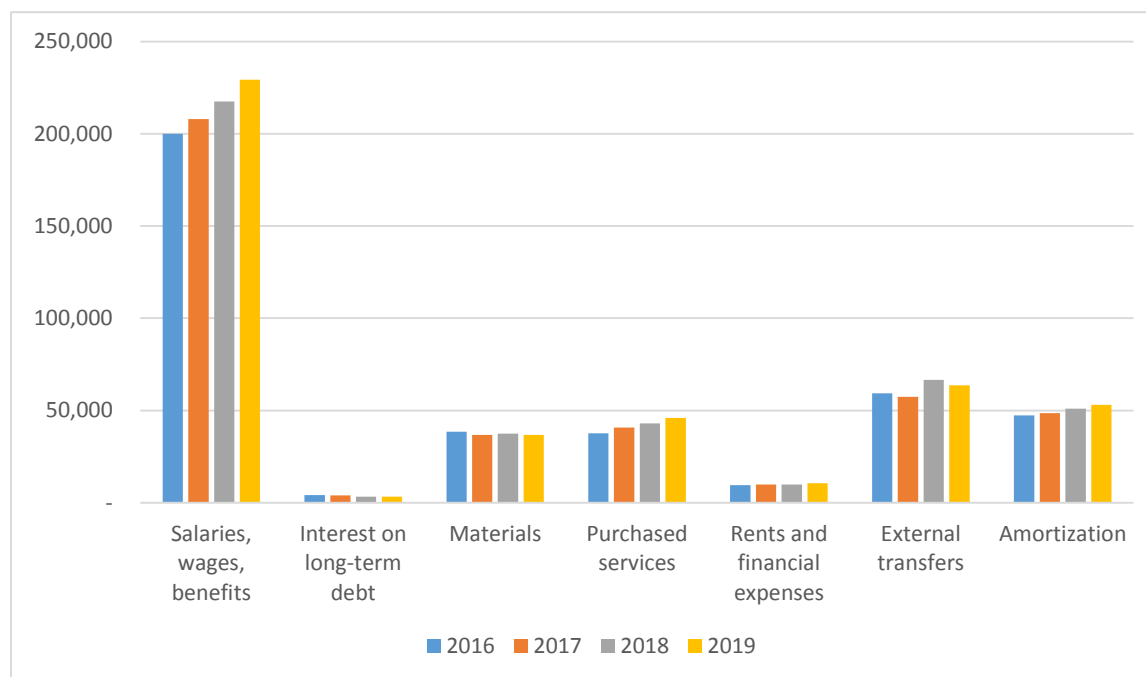
Government business enterprises earnings

Government business enterprise earnings increased by \$27.2 million. Of the \$34.0 million in government business enterprise earnings reported in 2019, \$1.1 million is GJR's net income. The remaining \$32.9 million is GMHI's net income of \$41.8 million less \$8.8 million in the refundable portion of deferred tax liability associated with the merger transaction between GMHI and Alectra.

Expense Highlights

Year-over-year total expenses increased by \$13.5 million with the largest increase in the salaries, wages and employee benefits cost (\$11.7 million), purchased services (\$2.8 million), and amortization of tangible capital assets (\$2.1 million). A decrease of \$3.0 million in external transfers offset these increases.

Figure 3 – Expenditure by type (in millions)



Salaries, wages and employee benefits

Salaries, wages and employee benefits are the most significant component of the City's operating costs, increasing by \$11.7 million (5%) over 2018. The increase is due to increased wage rates, increased employee benefits costs (OMERS, medical and dental, accumulated sick leave and retiree benefits) and costs from the

additional full-time equivalents hired. Slightly over \$3 million of the increase was related to the WSIB liability adjustment.

Materials

Materials expenses increased by \$785 thousand over 2018 with the largest drivers of this increase being contracted construction, automotive parts, and fuel costs due to fleet growth, increased use, and typical annual fuel commodity price increases.

Purchased services

Purchased services expenses increased by \$2.8 million over 2018 mainly due to increased activity for work related to monitoring, maintenance, remediation and rehabilitation such as increased storm water pond monitoring, maintenance on storm water linear system, clean-up of contaminated sites, and water valve maintenance.

External transfers

External transfers decreased by \$3.0 million under 2018, mainly due to a very large increase in TIBG expenses in the prior year (2018 was \$12.0 million and 2019 was \$1.6 million). This was offset by an increase in transfers to the County of Wellington for Child Care services (\$4.3 million increase) and Ontario Works (\$800 thousand increase); 2019 external transfers also included \$400 thousand for the Smart Cities Program.

Figure 4 below depicts the percentage amount of total operating expenses for each service category within the City for 2019 and Figure 5 presents the same information for 2018. The percentages have remained relatively stable with a slight increase in protection services, general government and recreation and cultural services and decreases in social housing and planning and development. The most significant year-over-year change was the decrease in planning and development which was the result of the significantly lower TIBG expense in 2019.

Figure 4 – Expenses by Function (2019)

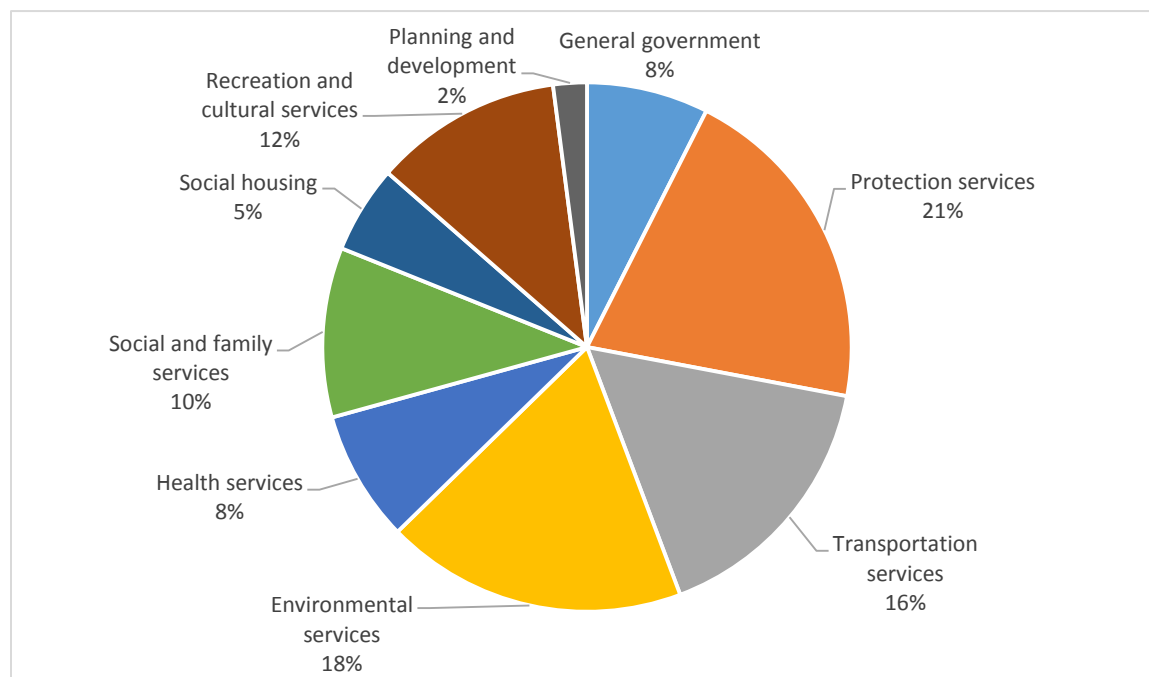
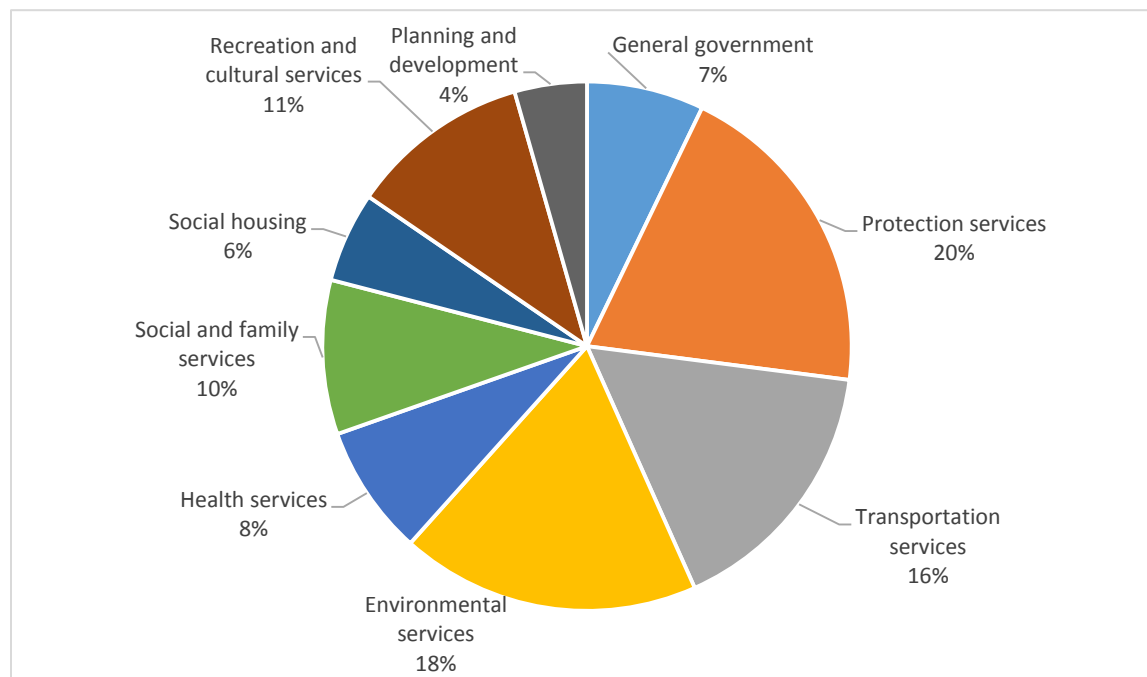


Figure 5 – Expenses by Function (2018)



Accumulated Surplus

Accumulated surplus is the excess of the City's total assets over its total liabilities. A full breakdown of the accumulated surplus can be found in Note 14 to the Consolidated Financial Statements included in Attachment-1. The most significant component of the accumulated surplus is the amount invested in tangible capital assets, followed by the City's reserves and reserve funds which are detailed in Schedule 4 of Attachment-1.

The 2019 Year-end Reserve and Reserve Fund Statement (report 2020-39) was approved by Council in May and provided an overview of current reserve balances, activity throughout the year, outstanding commitments and target reserve levels.

Statement of Cash Flows

This statement provides a summary of how cash was generated during 2019 and where it was spent. The purpose of this statement is to reconcile the excess of revenue over expenses for the year from the Statement of Operations and Accumulated Surplus to cash on hand at the end of the fiscal year, as shown in the Statement of Financial Position.

The first section of the Statement of Cash Flows highlights the cash earned from operations and begins with the excess of revenues over expenses for the year of \$84.8 million, and adds and subtracts items that are non-cash in nature. During 2019, the City and its consolidated entities generated \$102.2 million in cash from operations (2017 - \$123.1 million).

The next two sections relate to capital, investing, and financing activities which show how the City has used and generated its cash during the year. The City spent \$88.8 million to acquire tangible capital assets, and received \$2.4 million from the sale of capital assets. Net cash of \$75.4 million was transferred to the City's investment accounts, and the City received dividends totaling \$15.7 million from its government business enterprises (GMHI and GJR). A further \$2.5 million was

transferred to the City's investment accounts from GMHI and is accounted for as a loan from GMHI to the City. The City issued debt in 2019 totaling \$33.1 million and The Elliott borrowed \$1.4 million on a line of credit but total debt principal repayments totaling \$13.9 million were made during the year, for a net cash inflow from debt activities of \$20.5 million. Receipts of deferred contributions (development charges, federal and provincial gas tax, and Ontario Building Code and parkland dedication revenues) exceeded expenditures funded through these sources by \$25.9 million

Overall, the City's cash position increased year-over-year by \$4.7 million.

Review of the Consolidated Entities' Financial Statements

In the preparation of the 2019 Consolidated Financial Statements, staff reviewed the audited Financial Statements for each of the consolidated entities. The impacts of the consolidated entities' Financial Statements on the City's Consolidated Financial Statements are included in the commentary above, however an overview of significant items from the consolidated entities financial statements is provided for further information:

The Elliott (Attachment-2)

The Elliott is required to be consolidated into the City's Financial Statements because of its financial reliance on the City. The Elliott's Financial Statements are audited by KPMG LLP and have a year-end date of December 31, 2019. KPMG provided a clean audit opinion on The Elliott's 2019 Financial Statements.

The Elliott reported an annual surplus of \$1.2 million for 2019 (2018 - \$1.1 million). The net deficit of \$5.8 million at the beginning of the year was reduced to \$4.6 million by the end of the year. Operating revenue increased by approximately \$300 thousand and operating expenses increased by approximately \$450 thousand, however bequests totaling \$290 thousand were received during the year offsetting what would have otherwise been a decrease in the annual surplus.

The City has a loan receivable from The Elliott of \$14.7 million (2018 - \$15.3 million) relating to debentures issued on behalf of The Elliott by the City. The loan was eliminated in the consolidated statements, but is highlighted here because it appears on The Elliott's Financial Statements. The City guarantees The Elliott's line of credit totaling \$1 million, as well as a revolving lease line of \$2 million, of which \$1.4 million was drawn upon at the December 31, 2019 year-end (2018 - \$0). On June 29, 2020, Council approved an increase in the amount of revolving lease line of credit it would guarantee for The Elliott from \$2.0 million to \$4.0 million.

DGBA (Attachment-3)

The DGBA is a business improvement area in the City and is consolidated because it is financially dependent on the City for funding. The DGBA Financial Statements are audited by KPMG LLP. KPMG provided a clean audit opinion on the DGBA's 2019 Financial Statements.

The DGBA reported a 2019 excess of revenues over expenses of \$8 thousand compared to \$51 thousand in 2018. In 2019 net assessment write-offs were \$13 thousand, whereas recoveries of \$4 thousand were reported on the same line in 2018. Special projects contributions also increased by \$22 thousand in 2019.

Public Health (Attachment-4)

The City proportionately consolidates the assets, liabilities, revenues and expenses of Public Health based on the percentage of municipal funding contributed during the year. The 2019 percentage was unchanged from 2018 at 46.3%. This percentage is based on the 2016 census population. The Public Health Financial Statements are audited by KPMG LLP. KPMG provided a clean audit opinion on Public Health's 2019 Financial Statements.

Public Health reported an excess of revenues over expenditures of \$805 thousand (2018 - \$325 thousand) and an increase in the accumulated surplus from \$17.0 million in 2018 to \$17.8 million in 2019. The largest portion of the accumulated surplus is invested in tangible capital assets (net of long-term debt used to finance Public Health's two owned facilities), with just over \$1.1 million in reserves and reserve funds at the 2019 year-end (2018 \$5.7 million).

The City has a loan receivable from Public Health of \$2.5 million (2018 - \$5.3 million). This loan is eliminated in the consolidated statements but is highlighted here because it appears on Public Health's Financial Statements.

GMHI and GJR

GMHI and GJR both have a formal process for reporting their Financial Statements to Council in accordance with each entity's Shareholder Declaration; for this reason their Financial Statements have not been included as attachments. Commentary is provided in the Council reports that accompany these statements which Council will receive at each company's annual general meeting on July 22, 2020.

Police Board

The Police Board is fully consolidated into the City's Consolidated Financial Statements and a supplementary schedule (Schedule 6) within Attachment-1 outlines the activity throughout the year. An analysis of the Police Board's variance is included in the Council quarterly and annual variance reporting, so further analysis is not provided in this report.

Library Board

The Library Board is fully consolidated into the City of Guelph's Consolidated Financial Statements and a supplementary schedule (Schedule 5) within Attachment-1 outlines the activity throughout the year. An analysis of the Library Board's variance is included in the Council quarterly and annual variance reporting, so further analysis is not provided in this report.

External Audit Findings Report

The external audit results, as prepared by KPMG LLP, are included in Attachment-5. Highlights from KPMG's report include:

- There were no significant changes from the Audit Planning Report previously presented to Council.
- There have been no initial selections of or changes to significant accounting policies and practices to bring to Council's attention.
- No significant control deficiencies in internal control over financial reporting were identified.
- No audit differences were identified by KPMG.
- KPMG confirmed their independence from the City.

Financial Implications

An unqualified opinion of the 2019 Consolidated Financial Statements will assist the City in obtaining a fair credit rating which has the potential to lower its borrowing costs as well as support grant-funding requests from outside organizations.

Consultations

No consultations were required.

Strategic Plan Alignment

The City's Consolidated Financial Statements and the unqualified audit opinion provided by KPMG LLP on them supports the Strategic Plan pillar of Working Together for our Future through maintaining a fiscally responsible local government.

Attachments

Attachment-1 City of Guelph 2019 Consolidated Financial Statements

Attachment-2 The Elliott Community 2019 Audited Financial Statements

Attachment-3 Downtown Guelph Business Association 2019 Audited Financial Statements

Attachment-4 Wellington-Dufferin-Guelph Public Health 2019 Audited Financial Statements

Attachment-5 City of Guelph 2019 External Audit Findings Report

Departmental Approval

None noted.

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