TBS

Office of the Provincial Controller Division

Accounting Updates

Briefing for the Secretary of Cabinet

March 16, 2018

CONFIDENTIAL DRAFT FOR MARCH 14 DEPUTY MINISTER PRE-BRIEF
FOR DISCUSSION PURPOSES ONLY

Topics for Discussion

1. Accounting Issues Update
2. Fair Hydro Plan
3. Pre-Election Report
4. OPCD Internal Control Review
5. Other Updates

1. ACCOUNTING ISSUES UPDATE

Accounting Issues – Update

Items potentially affecting 2017-18 Surplus/Deficit

	Issue	Potential Impact	Update	Impact to 2018-19 and out years
1	Indigenous Settlements/ Contingent liabilities	TBD (based on future assessment)	• A working group has been established to develop a framework to identify, assess and track OPS legal litigation/negotiation claims to support OPS financial reporting for likelihood/estimable under PSAS. • Analysis has been completed to assess the impact on the interim numbers. Ministries (MAG, MIRR & MNRF) will continue to assess the likelihood/impact of the contingent liabilities, subsequent to March 31.	• Yes – TBD (contingent liability framework to be implemented)
2	OPG & H1 - H1 – Control Assessment - H1 – OEB Appeal - OPG – Asset Retirement Obligations	No change in 2017-18 resulting from control assessment ~$440M lower revenue prior to appeal $100M lower for 2017-18 & 2018-19; $225M lower in 2019-20	• Hydro One control assessment with ownership <50% determined H1 is controlled for 2017-18; 2018-19 at risk and reassessment will be performed with ownership further reduced resulting from Avista transaction • H1 update on OEB appeal re: decision to share portion of deferred tax asset with ratepayers; appeal heard by OEB February 12, no estimated timeframe for ruling; H1 did not provide any provision in Q4 update released in February • OPG has provided updates for ARO; declining discount rates based on 15 year rolling average; lower ARO estimates due to extended useful life of Pickering units	• Yes – potential impact if a change in control assessment exists; range $75M-$175M assuming current dividend per share unchanged • Yes – if not ruled before release of 2017 -18, one-time adjustment based on outcome of appeal • Yes – updated annually
3	Accruals for negotiated compensation	$50M (MOHLTC)	• No accrual expected related to on-going negotiations for MAG/MCSCS for 2017-18; • MOHLTC (OMA) has included $50M for 2017-18 as part of their year-end accrual for physician services; binding arbitration process in late 2018 if no agreement	• Yes –final settlement will be reported

Accounting Issues – Update

Items potentially affecting 2017-18 Surplus/Deficit

	Issue	Potential Impact	Update	Impact to 2018-19 and out years
4	Drug rebates (MOHLTC)	~$345M (revenue - prior year recovery)	• Correction of cutoff error identified in 16-17 audit (3 month lag); pickup of extra quarter of rebates ($259M for MOHLTC; $86M for MCYS)	• No – one-time correction
5	Non-resident Speculation Tax	$194M Interim estimate	• Position paper drafted supporting recognition of NRST when collected with a provision for rebates to be paid based on actual data and reasonable estimates; awaiting OAGO confirmation	• Yes – TBD (OEP)
6	Waterfront Toronto	~$24M (Phase 1 only)	• Accounting model finalized for Phase 2 of WT to report as transfer payment to City of Toronto (no provincial interest). • Additional expense managed within.	• Phase 1: ~ $13M • Phase 2: ~ $400M (managed within)
7	Remedy	$150M lower expense	• Matter not settled at mediation – EDU lowered estimate based on additional information pertaining to likelihood of ETFO application	• Potential – final settlements paid
8	GGRA transfer payment agreements	• TBD	• OPCD will review draft TP agreements to determine whether they meet the criteria for accrual in current year	• Potential
9	Six Nations Agreement	• $102M	• OPCD working with MOF to evaluate accounting for draft agreement	• No – one-time impact
10	Non tax revenue	~$100M higher revenue	• Plan to ensure revenue to March 31 recorded for other tax revenue subsequent receipts (e.g. EHT); historically, there has been a cut-off error	• No – one-time correction

Accounting Issues – Update

Items affecting 2018-19 and beyond

	Issue	Update
1	Northern Grid (Watay)	• Assessment of any potential risk on loan default will result in loan provision to be reported, as well as any amounts guaranteed under the Aboriginal Loan Guarantee Program for FN equity investment • Province is assuming construction risk throughout project through specific milestones related to community connectivity; need to assess annually for potential loss provision
2	Pension Updates	• Updates based on actuarial data from plans: $32M in 2018-19; ($162M) in 2019-20; ($388M) in 2020-21; ($353M) in 2021-22; the lower expense is due to higher than expected investment returns and lowering of the salary escalation expectation
3	Transit Infrastructure	• City of Toronto and Metrolix Agreement-in-Principle signed for LRT/RER • OPCD will be engaging external advisor to support development of a framework to support determination of ownership for regional transit projects; MTO and Metrolinx are supporting these efforts
4	Ontario Cannabis Retail Corporation	• Based on the accounting analysis performed, the entity will be recognized as a Government Business Enterprise for financial reporting purposes. • Investments in Government Business Enterprises are included in the government's consolidated financial statements using the modified equity method (one-line consolidation with additional disclosure in Schedule 9). • Estimated $22M in set-up costs to be incurred by the LCBO and recovered ($6M in capital) – to be updated for year-end
5	Accounting for pre-2008 tax appeals	• OPCD reviewing MOF accounting for tax appeals and whether accruals as a contingent liability is appropriate – currently recorded when appeal is lost vs. estimating outcome

Accounting Issues

- Indigenous Settlements
  - Process underway with MAG/MIRR regarding development of a principled framework for risk assessment and cost measurement for on-going litigated and negotiated events that may impact the current practice for recording contingent liabilities in the financial results.
    - Quarterly updates with mandates > $20M to be brought to TB for approval
    - Establish consistency and rigour to evaluation of contingent liabilities; framework presentation to Provincial Controller/DMs in April 2018
  - Reviewing negotiating mandates being brought to Treasury Board to ensure fiscal impacts, timing and risks are applied consistently (e.g. flooding easements, land valuation)
- Hydro One / Ontario Power Generation
  - OEB decision pending with possible negative impact to results for Hydro One re: deferred tax assets resulting from PILs exit (impact to Province ~$440M)
    - Appeal heard February 12; no timeframe for ruling – 2017-18 impact if settled before release
  - KPMG has supported the control assessment of H1 under PS1300 at less than 50% ownership; increased risk of portfolio investment accounting in 2018-19 after Avista issue with lowering stake ~ 42%; will be revisited annually
  - OPG has completed its annual exercise to update estimate cost of asset retirement obligation; lower costs mainly due to extended useful life of Pickering units

	2017-18	2018-19	2019-20	2020-21
ARO Obligation under IFRS ($M)	300	375	475	425
Discount Rate	4.1%	4.3%	3.9%	3.8%

Accounting Issues

- Watay/Northern Grid
  - Assessing risk of default on loans to fund construction for northern grid connection to be repaid by future federal contributions upon commercial in-service (proposed staging)
  - Province to guarantee a portion of borrowing for the capital contribution for First Nations through the Aboriginal Loan Guarantee Program
  - Loan repayments to be secured through federal transfers to Watay upon completion of key milestones (“substantial completion” – 8 communities; “completion” – full connectivity)
- Transit Infrastructure
  - Discussions are continuing with MTO, Metrolinx on the planning decision history surrounding regional transit projects
  - OPCD will be engage an external advisor to assist with the development of a framework which can be applied (retrospectively and prospectively) is assessing project design in the context of PS3150 – Tangible Capital Assets
  - Work will also include governance model (e.g. TransLink in BC)
  - The OAG has identified accounting for transit infrastructure as a focus for the 2017-18 audit.
- Ontario Cannabis Retail Corporation (OCRC)
  - In October 2017, Ministry of Finance (MOF) received TB/MBC approval to establish a non-share capital corporation that is a Crown agency, the OCRC, which will have a subsidiary relationship to the Liquor Control Board of Ontario (LCBO).
  - Based on the accounting analysis performed, similar to LCBO, OCRC will be recognized as a Government Business Enterprise for financial reporting purposes. Government Business Enterprises carry on a business which sells goods and services and is self-sustaining from outside revenues; can be a participant in a lawsuit (sue or be sued) – consolidated on a one-line modified equity method.
  - Estimated $22M in set-up costs to be incurred by the LCBO and recovered ($6M in capital) – to be updated for year-end.

Accounting Issues

- Compensation
  - Current negotiations with ALOC/OCAA (MAG) – expired June 30/17 and OPSEU Corrections Bargaining unit (MCSCS) – expired December 31/17; negotiations on-going
  - MOHLTC has a negotiating mandate for a contract starting April 1, 2017; no amounts related to negotiations were accrued in 2016-17
  - Reasonable estimates for amounts relating to a negotiated settlement involving 2017-18 should be accrued as a contingent liability (PS3300); MAG/MCSCS have indicated no accrual will be made for 2017-18; MOHLTC has included $50M for 2017-18 to align with mandate of 2.6%

- Non-resident Speculation Tax
  - Tax applied on interest in specified residential properties for non-residents, subject to rebate eligibility under certain conditions
  - Criteria being evaluated under PSAS to determine the "taxable event" for recognition; initial determination that revenue should be recognized when collected on a net basis against assessment for rebates eligible for claim (actual claims or estimate)
  - Position paper shared with OAGO for comment/confirmation of recognition for 2017-18

2. FAIR HYDRO PLAN

Fair Hydro Plan

- Key agreements have been drafted to facilitate the issuance of the debt to the market and establish the terms of the provincial guarantee to fund the Global Adjustment
    - Agreements provide for OPG as the Financial Services Manager to retain independence on the individual debt issues while constrained within the Financing Plan that is submitted to the Minister of Energy
- Under IFRS10, the current agreements support accounting for the financing trust to be consolidated under OPG, and brought into the government financial statement on a one-line presentation for government business enterprises
- OPCD is finalizing a position paper which documents all the facts, considerations and professional judgments applied in arriving at the accounting for the FHP as it relates to the GA as a rate regulated asset under US GAAP, the consolidation of the trust, and the impact on the Province's consolidated financial statements
    - Once finalized, this paper will be shared with the OAGO and the Chair and Director of the Public Sector Accounting Board

3. PRE-ELECTION REPORT

Pre-Election Report

- OAGO has begun to request information (revenue/expense)
  - 5-year historical plan/actuals from each Budget year

- Standards to be applied for future oriented information – Section 4250 (Part V – CPA Handbook) and AuG-6 (Canadian Assurance Standards)

- As part of Management's Representation, the audit standards require that "the assumptions underlying the forecast reflect management's judgment as to the most probable set of economic conditions and the company's planned courses of action for (period). These assumptions are supportable and consistent with the plans of the company, and are reflected in the forecast. All such assumptions have been disclosed to you (the Auditor)".

Attestation - Current Situation

- As part of the development of the Pre-Election Report (PER) Treasury Board Secretariat and the Ministry of Finance will be required to provide a management representation letter to the Auditor General providing assurance that:
  - The report is in compliance with the Fiscal Transparency and Accountability Act, 2004.
  - All relevant information has been disclosed to the Auditor General.
  - All assumptions made are supportable and consistent with government policy decisions, economic forecasts and the government's anticipated actions over the coming three years.
- The letter will be signed by TBS and MOF Deputy Ministers, Associates, Chief Economist, Provincial Controller and the CEO of the Ontario Financing Authority.
- In support of the representation letter, TBS will be requesting each Ministry CAO and Finance Director provide supporting assurance with respect to their approach and assumptions made in their 2018-19 PRRT submissions.

4. OPCD INTERNAL CONTROL REVIEW

Current Situation

- In July OPCD issued a Request For Services to:
  1. Confirm the alignment of OPS Internal Control Framework with the COSO 2013 international standard, and;
  2. Review and assess OPCD controls over financial reporting processes including:
     - Certificate of Assurance
     - Consolidation activities
     - Pension reporting
     - Period Close processes
     - Post-Close activities
     - Provision of complex accounting advice.
- PwC has completed their assessment and have submitted their final report to OPCD.

Findings

1. Internal Control Framework Assessment
   - is based on widely adopted standards
   - has been thoroughly tested and widely understood
   - implementation plan is aggressive but OPCD has considered the need to maintain momentum and the size and complexity of the OPS
   - the inclusion of annual progress reports should help OPS manage timeline and assess if additional support is required
   - opportunity to continue building training programs to support knowledge and awareness

Findings

2. Review and assess OPCD controls over financial reporting
   - Documented business processes, risks and controls
   - Tested 41 identified controls
   - Overall found controls are in place to address key risks within the organization
   - Identified 21 improvement opportunities related to:
     - Providing additional review over control activity
     - Provide additional documentation to evidence presence of control activity
   - Identified one control not implemented effectively however noted that plans have been put in place to address this going forward.
   - Noted OPCD is addressing future process changes through identifying future control requirements (e.g. CHIRP implementation)

Next Steps

- Assess improvement opportunities
- Develop project plans and implement

5. OTHER UPDATES

Other Updates

- PSSD Automation
  - We have utilized portal/web based technology to enable accountable organizations to populate their employee records in one tool that provides automated data validation. This stream lines the whole manual process of submitting spread sheets requiring manual validation by both the ministries and OPCD
- Planning, Budgeting and Forecasting (PBF)
  - The PBF initiative will enable the integration of the Planning, Budgeting & Forecasting processes with in IFIS. The solution will capture the data once at the lowest level and provide the ability to roll-up, report and manage multiple structures required by the central agencies and ministries (Estimates, PRRT, Operational and Scenario Planning)
- CHIRP
  - Hyperion-based solution to automate and standardize the production of the consolidated financial statements
  - Currently in final testing phases, and will undergo an end-to-end test in September 2018 (recreate 2017-18 consolidated financial statements); system of record for 2018-19 PA
  - Ministry training and impact assessment process for those affected – in development
- Enterprise Risk Management
  - Scheduled update with Chair of Corporate Audit Committee Apr 5
  - ERM Executive training program scheduled April 25th
- Finance Community Talent Management
  - Executive Development Committee presentation June 2018