TBS

Office of the Provincial Controller Division

Accounting Updates

Briefing for the Secretary of Cabinet

February 16, 2018

CONFIDENTIAL DRAFT FOR FEBRUARY 7 ASSOCIATE 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

1. ACCOUNTING ISSUES UPDATE

Accounting Issues – Update

Items potentially affecting 2017-18 Surplus/Deficit

TBS

	Issue	Potential Impact	Update	Impact to 2018-19 and out years
1	Indigenous Settlements/ Contingent liabilities	TBD	• 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 targeting February 2018 • Assessing potential fiscal impacts/timing of negotiating mandates First Nations regarding flooding rights and other settlement costs (including AOO treaty) • **Potential impact for 2017-18 – TBD**	• Yes -- TBD
2	OPG & H1 - H1 – Control Assessment - H1 – OEB Appeal - OPG – Asset Retirement Obligations	TBD	• Finalizing control assessment with ownership <50% of Hydro One; early indication is controlled for 2017-18; 2018-19 at risk; **impact to revenue as investment - TBD** • H1 update on OEB appeal re: decision to share portion of deferred tax asset with ratepayers; appeals heard by OEB February 12, H1 to release Q4 results Feb 13 – **potential impact of reduce revenue ~$440M** • OPG has confirmed discount rate associated with ARO under IFRS (no change from prior year); estimate for ARO costs update in Feb 2018	• Yes -- TBD
3	Compensation negotiations – OMA	TBD	• OMA negotiations on-going relating to fee-for-service; pending discussions with MOHLTC to get an update and determine if any amounts related to 2017-18 will be negotiated as a retroactive or lump-sum payment which can be reasonably estimated requiring accrual. • Preliminary accrual estimate - **TBD**	• Yes -- TBD
4	Non-resident Speculation Tax	~ $150M	• Position paper drafted supporting recognition of NRST when collected with a provision for rebates to be paid based on actual data and reasonable estimates; **to be shared with OAGO**	• Yes -- TBD
5	Pension Updates	TBD	• All actuarial data received; updates in process and expected to be complete by mid-February	• Yes -- TBD

Accounting Issues – Update

Items potentially affecting 2017-18 Surplus/Deficit

	Issue	Potential Impact	Update	Impact to 2018-19 and out years
6	Drug rebates (MOHLTC)	• TBD	• Identified during 2016-17 audit that drug rebates were not accounted for on a fiscal year basis (3 month lag); working with MOHLTC to ensure that an appropriate estimate for the rebate is recorded correctly	• Yes -- TBD
7	OSAP	~ $50M	• MAESD forecasted net grants to students taking into consideration the percentage of grants they expected to recover for non-compliance (revert to loan status) -- not in accordance with PSAS; future periods will see recoverable grants reported as revenue (prior year recovery)	• To confirm if the PRRT reflects the confirmed accounting method
8	Waterfront Toronto	• TBD	• Accounting model finalized for Phase 2 of WT to remove timing gains/losses for non-congruent contributions from the federal and municipal governments; **impact of adjustments being confirmed**	• Yes
9	Remedy	• TBD	• Matter not settled at mediation – OPCD working with EDU to obtain re: details of mediation re: split between positions to assess whether remaining accrual is sufficient	• Potential
10	GGRA transfer payment agreements	• TBD	• OPCD will review draft TP agreements to determine whether they meet the criteria for accrual in current year	• Potential
11	Accounting for tax appeals	• TBD	• 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	• Potential
12	Six Nations Agreement	• TBD	• OPCD working with MOF to evaluate accounting for draft agreement	• Potential
13	Non tax revenue	• TBD	• 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

Accounting Issues – Update

Items affecting 2018-19 and beyond

	Issue	Update
1	**Northern Grid (Watay)**	• Supporting MOE/OFA on accounting implications/risks of loan financing plan to connect northern communities to electricity grid (i.e. Watay) to be repaid through future federal contributions at key milestone project dates • 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
2	Transit Infrastructure	• 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
3	Ontario Cannabis Retail Corporation	• Finalizing classification of the new entity created in December 2017 under PSAB (as an other government organization or government business enterprise) based on business objects, expectations • Estimated $22M in set-up costs to be incurred by the LCBO and recovered ($6M in capital) – to be updated for year-end • Status will determine final presentation for Public Accounts (one-line consolidation with additional disclosure in Schedule 9 or full line-by-line consolidation)

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 Controllers/DMs in February 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
  - H1 disclosed $885M potential negative impact to results at Q3 regarding OEB decision re: deferred tax assets resulting from PILs exit (impact to Province ~$440M)
    - Currently under appeal; hearing to occur by 3rd week of January
  - KPMG has been provided with information from MOF to assist in assessing control under PS1300; expect to be finalized in late January/early February
  - OPG is undertaking annual exercise to update estimate cost of asset retirement obligation (expected February 2018); no material change in prescribed discount rate (2017-18 vs. 2018-19)

	2017-18	2018-19	2019-20	2020-21
Discount rate	4.30%	4.15%	3.95%	3.85%
ARO Obligation under IFRS ($M)	400.0	475.0	700.0	750.0

Accounting Issues

- Wataay/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 Wataay 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.

- Healthcare of Ontario Pension Plan
  - HOOPP increased benefits for past service which resulted in approximately $190M - $200M in added expense which was offset by the valuation allowance taken against the net pension assets position of the plan under accounting rules
    - The Pension Asset Expert Advisory Panel recommended taking the provision against HOOPP and CAATPP pension as the Province had no demonstrable control over them (unlike the jointly-sponsored OTPP and OPSEUPP)
  - The Province will continue to maintain a dialogue with HOOPP on how the Province accounts for its share of the defined benefit plan and the impacts of plan changes on government accounting

Accounting Issues

- Compensation – Ontario Medical Association
  - Current negotiations between the OMA and MOHLTC are on-going
  - At last year's Public Accounts, MOHLTC confirmed the negotiating mandate was for a contract starting April 1, 2017; no amounts related to negotiations were accrued in 2016-17
  - Status of negotiations needs to be updated (to discuss with MOHLTC); reasonable estimates for amounts relating to a negotiated settlement involving 2017-18 must be accrued as a contingent liability (PS3300)

- 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 to be shared with OAGO for comment

Accounting Issues

- Ontario Cannabis Retail Corporation (OCRC)
  - Entity will be operational in 2018 (established Dec 2017); determination underway if the organization will meet the conditions for a government business enterprise (similar to LCBO) or whether it will be consolidated as an other government organization
    - 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
    - Other Government Organizations are entities controlled by the government and are consolidated on a full (line-by-line) basis (revenues, expenses, assets, liabilities)
  - Currently operating under LCBO with start-up costs to be reimbursed once operations commence (initial estimate of $22 million ($6M capital), to be updated by MOF)

- Related Party Transactions
  - PSAB Standard PS2200 Related Party Disclosures to apply to fiscal years beginning on or after April 1, 2017. (2017-18 Public Accounts)
  - Disclosure is generally required when related party transactions have occurred at a value different from that which would have been arrived at if the parties were unrelated and would have a material impact to the financial statements (professional judgment).
  - Leveraging existing financial disclosure process established for key management personnel involved in planning, directing and/or controlling activities (e.g senior management, Deputy Ministers and Ministers) and documenting the applicable conflict of interest processes; and identify and supplement controls where needed.
  - For public service employees, attestation of negative confirmation will be obtained through the Certificate of Assurance process (leveraging the requirements under PSOA); engaged political staff contacts through CO and the Office of the Integrity Commissioner to document process for disclosures

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 Deputy Minister and CAO 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