TBS

Office of the Provincial Controller Division

Accounting Updates

Briefing for the Secretary of Cabinet

January 19, 2018

CONFIDENTIAL DRAFT FOR PRE-BRIEF
FOR DISCUSSION PURPOSES ONLY

Topics for Discussion

1. Accounting Issues Update
2. Fair Hydro Plan
3. Scarborough Subway Extension
4. OPCD Internal Control Review

1. ACCOUNTING ISSUES UPDATE

Accounting Issues – Update

Items potentially affecting 2017-18

	Issue	Update
1	Indigenous Settlements / Northern Grid	• Contingent liability framework to assess litigation and negotiated settlements (in advance of litigation) 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
2	OPG & H1 - H1 – Control Assessment - H1 – OEB Appeal - OPG – Asset Retirement Obligations	• Finalize control assessment with ownership <50% of Hydro One by end of January • H1 update on OEB appeal re: appeal decision to share portion of deferred tax asset with ratepayers; update to be received week of Jan 22 –impact of lower income ~ $440M • OPG has updated discount rate associated with ARO; estimate for ARO to update in January 2018
3	Grassy Narrows - Trust	• Trust in the process of being established under the guidance of the legislation • Control and consolidation assessment to be determined and shared with AG once structure is more defined; more details available after FN/Panel meeting scheduled for end of January. • Structure will not affect reported $85M expense; presentation only
4	Compensation negotiations – OMA	• OMA negotiations on-going relating to fee-for-service; discussions with MOHLTC to get update and determine if any amounts relate to 2017-18 and will be negotiated as a retroactive or lump-sum payment which can be reasonably estimated and accrued. • Preliminary accrual estimate - $260M
5	Non-resident Speculation Tax	• Discussions with MOF re: tax remittances from non-residents on real estate and identification of the “taxable event” which would determine the timing of revenue recognition (impact of rebate eligibility) • Potential for revenue of up to ~$150M (based on estimate to December 31)
6	Related Party Transaction Disclosure (PS2200)	• New accounting standard issued effective April 1, 2017 requiring disclosure for material transactions • Reporting attestations in development for public service and political staff • Disclosure only – no financial impact

Accounting Issues – Update

Items affecting 2018-19 and beyond

	Issue	Update
1	Hospitals of Ontario Pension Plan	• Met with team from HOOPP to review potential impact of plan changes to the Province's fiscal plan as a defined benefit pension plan • Presentation to HOOPP Board on accounting for HOOPP in the Public Accounts (March 2018)
2	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 • Future 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
3	OPG – Asset Retirement Obligations	• OPG has updated discount rate associated with reporting ARO under IFRS; estimate for ARO to update in January 2018 (current estimated impact – 2017-18 - $425M, 2018-19 - $525M – consistent with last year)
4	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
5	Ontario Cannabis Retail Corporation	• Determination of status of new entity created in December 2017 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 / Northern Grid (Watay)
  - 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)
  - 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)
- 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 January 2018); no material change in prescribed discount rate (2017 vs. 2018)

	2017-18	2018-19	2019-20
Discount rate	4.3%	4.1%	3.9%
ARO Obligation under IFRS ($M)	425.0	525.0	675.0

Accounting Issues

- Grassy Narrows
  - Trust in the process of being established under the guidance of the legislation
  - Operational and administrative structures to be established
  - Control and consolidation assessment will be required after the structure is more defined

- 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 Currently engaging political staff contacts to determine process for disclosures

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; discussions with MOF to understand program design in determining accounting treatment for 2017-18;
  - Expecting final resolution by end of January

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 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); engaging political staff contacts to determine process for disclosures through TBS DMO/CO

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 GA as a rate regulated asset under US GAAP
  - Once finalized, this paper will be shared with the OAGO and the Chair and Director of the Public Sector Accounting Board
- A presentation on the FHP accounting was made to the Chair, Director and staff of PSAB, as well as the Chair of the Accounting Standards Board (AcSB) in November 2017
  - A follow-up meeting has been requested in late January/early February

3. SCARBOROUGH SUBWAY EXTENSION

Scarborough Subway Extension

2013 Decisions

- The Scarborough Subway Extension (SSE) project first approved by City Council in late 2013 is continuing to be advanced by the City of Toronto/TTC through the initial concept development and early planning phase.
  - The project is a one-stop extension of the existing Line 2 (Bloor-Danforth Subway) from Kennedy Station to Scarborough Centre
- In 2013, Treasury Board approved the Province's role as a funding partner to the SSE under a Transfer Payment Agreement arrangement. Provincial accountabilities would be limited to flowing funding under a pre-defined construction schedule.

Allocation of risks between the City and the Province based on the approvals

- The current approval results in City of Toronto having:
  - Construction risk -- cost increases and overruns including for tunneling (currently increase estimated at >$1 billion), design/scope changes, penalties, delays, public impacts
  - Operational responsibilities and risks – on-time service, safety and security, delays
  - Policy responsibilities and risks – fare-setting, service levels
  - State of good repair responsibilities
- The Province's risk is limited to flowing funding under a pre-defined construction schedule.

Accounting by the Province based on approvals and allocation of risks

- Expense recognition for the transfer payment will occur when the eligibility criteria are met (e.g. costs incurred) and the payment is authorized.
- The accounting for the SSE must reflect the substance of the transaction -- a one-stop extension to an existing subway track, with the significant risks of ownership and operation with the City of Toronto. The Province does not own or control the asset.
- The funding arrangement, allocation of risks and accounting result are consistent with the Toronto-York Spadina Subway Extension, which is a 5 stop subway extension scheduled to open on December 17, 2017.

Alternatives which may be structured to achieve an extension to Scarborough Centre from Kennedy Station with Provincial capitalization and amortization of the asset

- If the Province owns and controls the TTC subway system
- If the Province builds an extension to a provincially owned and controlled asset (e.g. Eglinton LRT)

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