Office of the Provincial Controller

Financial Reporting Risks

December 9, 2016

Briefing to Secretary of Cabinet

DRAFT

Purpose

- To highlight immediate (2016-17) and longer-term (2017-18 and 2018-19) fiscal/financial reporting issues

- Communicate options and recommendations to address immediate high risk items

Immediate Issues -- Summary

	Issue	Fiscal impact in 2016-17	Reflected in FES	Multi-year impact
1	Pension accounting	$2.2 Billion	Yes	Yes
2	IFRS-US GAAP differences – OPG and H1	$1 Billion	No	Yes
3	Cap & trade proceeds	$478 Million	No	Likely not
4	Metrolinx MOU with City of Toronto (similar model for other transit projects)	TBD	No	Yes
5	Year-end transfers	TBD	No	Yes
6	Changes to consolidation (how and what)	N/A	No	Yes
7	Follow up audit – contaminated sites	TBD	No	Yes
8	Other GBE issues (H1 sale; unrealized gains/losses)	TBD	No	Yes
9	Reduced materiality by AG	N/A	N/A	N/A
10	Implementation of Hyperion Financial Mgmt	N/A	N/A	N/A
11	Earlier release of Public Accounts	N/A	N/A	N/A
12	Implementation of new accounting standards	N/A	N/A	N/A

1. Net Pension Assets

Risk:	High High profile issue; material forward-looking impact and/or volatility depending on nature and timing of co-sponsor agreements; relationship risk with co-sponsors and AG; audit risk if AG does not accept outcome inconsistent with her interpretation
Impact in 2016-17 (billions):	$ 2.2
Multi-year impact:	Yes -- $2.8B in 2017-18, $3.7B in 2018-19, and $3.9B in 2019-20
Impact included in FES:	Yes
Description of issue:	Accounting treatment for net pension assets of jointly sponsored and multi-employer pension plans -- OTPP, OPSEUPP, HOOPP and CAATPP
Current status/next steps:	• Expert panel has met twice - current focus on OTPP and OPSEUPP; • meeting scheduled with AG on Dec. 16; • Chair will be ready to brief OPCD/TBS/MOF/MO in early Jan 2017 and finalize report on OTPP/OPSEUPP by Jan 31, 2017. • HOOPP and CAATPP will be addressed in a supplement after January 31, 2017
Options under consideration:	a) If Panel agrees with Province re: recognition of net asset, Province will use guidance from Panel on measurement and engage a firm to value the asset; need strategy to work with AG on accepting findings of Panel b) If Panel does not agree with Province re: recognition of net asset, Province is assessing alternatives re: approaching OTF to meet the requirements set out by the Panel to recognize an asset (which may differ from the AG's interpretation)
Timing of expected resolution:	• Panel report back – January 9, 2017 • Panel report (OTPP/OPSEUPP) – January 31, 2017 • Asset valuations – February 15, 2017 (target) • Agreement with OTB (if required) – TBD
Province's ability to influence:	Province has ability to influence agreement with OTF should Panel not agree with Province's view.
Role of other ministries:	• EDU -- working through alternatives re: approaching OTF (e.g. changes to funding management policy) • Health & MAESD not currently engaged (not sponsors of HOOPP or CAATPP)

2. IFRS-US GAAP differences – OPG and H1

Risk:	High Audit risk (qualification for 2016/17 based on AG approach); lack of certainty w.r.t future IFRS standards for rate regulated accounting; transparency, accountability and VFM implications of 2 sets of books; AG Act implications of legislated accounting option
Impact in 2016-17 (billions):	$ 1.0 (based on AG's approach)
Multi-year impact:	Yes -- $100M in 2017-18, $ 100M in 2018-19, and $ 100M in 2019-20 (all based on AG's approach) Impact based on OPG's preferred approach -- $375M in 2016-17; $400M in 2017/18; $500M in 2018/19, $700M in 19/20
Impact included in FES:	No
Description of issue:	PSAB requires consolidation of OPG and H1 on an IFRS basis, whereas the Public Accounts reflects consolidation on a US GAAP basis, consistent with OPG and H1 external reporting as allowed by Securities Regulators and OEB
Current status/next steps	• Significant differences have historically been with OPG – working with OPG to refine estimates and assess ability to use OPG's preferred approach without a receiving a qualified opinion from AG; • Assessing whether it would be useful to approach PSAB again (response to OPS in 2016 connected any change to IFRS project on rate-regulated accounting, which is not scheduled for completion for several years)
Options under consideration:	(a) Continue to report OPG and H1 on a US GAAP basis in the CFS (legislate accounting; will result in qualified opinion unless AG Act also changed) (b) Approach PSAB for additional consideration; (c) Report OPG and H1 on an IFRS basis in the CFS (entities could continue to produce US GAAP financial statements for stand-alone financial statements) (d) Report OPG on IFRS and H1 on a US GAAP basis – historically significant differences have been in OPG; would leave publicly traded company (H1) with requirement to keep one set of books for now
Timing of expected resolution:	2017 Budget -Legislative changes could be considered as part of Spring Bill -Consider changes to basis of reporting for OPG/H1 to be reflected in Budget
Province's ability to influence:	Province is not able to influence PSAB or AG; If Province decides to consolidate OPG using IFRS, impact in year is estimated to be $375 million vs. $1 B
Role of other ministries:	Energy aware of ongoing considerations and stakeholdering with OPG and H1 OEFC involvement as necessary where potential impacts on f/s or audit opinion

3. Cap & Trade Proceeds

Risk:	High Timing of first auction in March 2017 results in settlement process straddling the year-end complicating timing of revenue recognition. Accounting model for new revenue stream requires consultation with OAG.
Impact in 2016-17 (billions):	$0.5
Multi-year impact:	No (although it is likely that if auction proceeds from March 22, 2016 auction are recognized in fiscal 2017-18, proceeds from 5 auctions will be recognized in fiscal 2017-18 as the last auction is 2017-18 is scheduled for February 2018 and the auction settlement process is expected to be complete by March 31, 2018)
Impact included in FES:	Risk not identified in the FES
Description of issue:	Assumptions regarding timing of revenue recognition for 2016 Budget in question. Based on preliminary accounting analysis, revenue likely to be recognized once emission allowances have been transferred to participant accounts. For the March 22, 2016 auction, this would mean that the related revenue is recognized in fiscal 2017-18.
Current status:	• OPCD working through comments on accounting analysis received from MOECC. • Accounting analysis to be shared with OAG in December to obtain preliminary feedback/concurrence for 2017 Budget.
Options under consideration:	• Unlikely that settlement process can be completed by March 31, 2017. • MOECC is providing additional information re: consideration of whether revenue recognition would be appropriate at auction certification date which occurs prior to the emission allowances being credited to the participant accounts (Auction certification date currently estimated as March 29, 2017)
Timing of expected resolution:	Mid-January/17 for feedback from OAG
Province's ability to influence:	If MOECC is able to move up the Auction date such that settlement process is complete by March 31, 2017, revenue would be recognized in 2016-17, subject to review by OAG.
Role of other ministries:	MOECC a key stakeholder and has provided background on C&T design, risks and rewards to the Province. Analysis has been provided to MOECC and MOECC has provided feedback. MOECC working through providing additional evidence supporting auction certification date as revenue recognition date for March 22, 2017 auction.

4. Metrolinx MOU with City of Toronto

(Note – model is being used for other transit projects as well)

Risk:	High Material potential impact on fiscal plan reflecting transaction with City as well as impact for future transactions for Mississauga and Hamilton assets (Hurontario LRT, Hamilton LRT
Impact in 2016-17 (billions):	$ TBD
Multi-year impact:	Yes (amounts TBD)
Impact included in FES:	No
Description of issue:	MOU contemplates the City taking responsibility for operations and maintenance of certain transit and also retaining the passenger revenue. The Province will retain lifecycle risk. It must be determined whether the Province maintains control of the transit assets (and therefore capitalizes and amortizes the assets over their useful lives) or whether the Province has substantively transferred the assets to the City of Toronto (which would be accounted for as a transfer and accelerate the recognition of the expense as compared to the capitalize and amortize model)
Current status:	Agreement in principle achieved between the Province and the City, including reference to funding for City from transit revenues.
Options under consideration:	Metrolinx engaging with external auditor regarding possible accounting opinion confirming Mx control.
Timing of expected resolution:	January, 2017
Province's ability to influence:	No provincial influence anticipated. Sharing of Mx accounting opinion with AG envisioned to confirm AG acceptance for CFS. (If AG disagrees, can make adjustments at corporate level).
Role of other ministries:	MTO, CPD engaged in discussions with MX on aspects of MOU and to ensure consistent understanding of anticipated accounting

Risks:
Multi-year impact: ($xxB in 2016-17, $xxB in 2017-18, $B in 2018-19, and $ xxB in 2019-20)

5. Year-end transfers

Risk:	Low/Med
Impact in 2016-17 (billions):	$ TBD
Multi-year impact:	Yes
Impact included in FES:	No
Description of issue:	Evolving view of AG regarding aspects of government year-end commitments and characteristics required to enable liability recognition in advance of signed formal TP agreement.
Current status:	OPCD engaging with OAG to discuss experience and lessons learned in advance of 2017 Budget Process.
Options under consideration:	Potential advice to ministries to mitigate risk: 1. Signed TP agreements in place by year-end 2. Flow funds by year-end Open discussion with OPCD and OAG to derive new guidance to be shared with Ministries. OPCD also engaging with OAG to clarify requirements (Jan/17).
Timing of expected resolution:	January 30, 2017
Province's ability to influence:	Reference to 2008 negotiated accountability provisions will be relevant. Collaboration with OAG to seek to establish common understanding.
Role of other ministries:	MOECC, others depending on planned 4Qis.

Risks (low to med): Minimal 4QIs expected in 2016/17

6. Changes to consolidation

Risk:	Low
Impact in 2016-17 (billions):	N/A
Multi-year impact:	Yes
Impact included in FES:	No
Description of issue:	AG recommendation that CASs, BPS be consolidated on the Province's books. Individual universities under assessment.
Current status:	Additional analysis required on impact if CASs were consolidated. No bottom line impact of line by line BPS consolidation, but revenues and expenses to change by amount of 3rd party revenue.
Options under consideration:	Under consideration for the 2017 Budget: - Consolidation of CASs - Consolidation of BPS sector (grossed up Rev/Expr) - Consolidation of single universities - Consolidation of Designated Administrative Authorities (DAAs)
Timing of expected resolution:	January/February
Province's ability to influence:	Provincial discretion as to whether to consolidate BPS as requested by the AG (presentation issue, no fiscal impact). Consolidation of individually controlled universities, CASs, DAAs which meet threshold tests required under PSAB (immaterial to SUDs, therefore no anticipated impact on audit opinion).
Role of other ministries:	MOF (OFA) to be involved to manage communications risks regarding consolidation MCSYS to provide details on CASs Sector Miniseries to provide details for Hospitals, school boards and colleges as well as Q&A input TBS Commas for Q&A (ALL) PEMD to provide details on DAAs.

7. Follow up audit – contaminated sites

Risk:	High
Impact in 2016-17 (billions):	No specific risk identified
Multi-year impact:	Yes
Impact included in FES:	No
Description of issue:	Expecting follow-up by AG on audit of implementation of contaminated sites standard. Any increases/decreases in liability will impact 2016/17 directly.
Current status:	OPCD communicating OAG planned review of contaminated sites. Draft policy under development.
Options under consideration:	Line and sector ministry readiness for AG review. OPCD policy guidance (format, timing, stakeholdering)
Timing of expected resolution:	Early January (post review by external firm)
Province's ability to influence:	Yes, own policy.
Role of other ministries:	MOECC input and direction to ministries in line with OAG audit findings from 2015. CPD role in supporting ministry estimates of ongoing costs.

Risks: Changes to estimates will impact in year (audit risk associated with computation), as well as results of AG VFM follow up audit which will to be reported in 2017 AG Annual Report.

8. Other GBE issues (H1 sale; unrealized gains/losses)

Risk:	Med
Impact in 2016-17 (billions):	TBD
Multi-year impact:	No
Impact included in FES:	Yes
Description of issue:	OPCD to engage with OAG on appropriate accounting and estimated errors (for SUDs). OEB Deliberations on benefit of Deferred Tax Asset (Province vs. Rate Payer)
Current status:	• Draft accounting for H1 sale to be reviewed by external firm (already provided). • Accounting for unrealized gains/losses to be discussed with OAG. • Potential share/cash acquisition under review. • OEFC to provide update on risks associated with potential OEB decision on benefit of deferred tax asset.
Options under consideration:	• Report all sales of H1 as revenue, ignoring inter-org transactions (immaterial) • Eliminate inter-organizational transactions. • Share/cash acquisition (TBD) to be accounted for under PSAB (OAG to be engaged) • Pending decision of OEB, ensure deferred tax benefit appropriately reflected on Province's books and Trillium Trust account.
Timing of expected resolution:	February, 2016 (decisions on eliminations/adjustments to be reflected in Budget)
Province's ability to influence:	Adjustments at discretion of the government (vs. SUDS impact)
Role of other ministries:	Information on H1 transactions to be received from Ministry of Energy and OFA.

Risks: Despite low anticipated $ amount of adjustments, commentary by AG in Annual Report for Audit Findings Report for any unadjusted differences could have reputational risk and also inadvertently impact Hydro One. Impact on amounts reported in Trillium Trust and AG commentary thereon also at risk.

9. Reduced materiality by AG

Risk:	High
Impact in 2016-17 (billions):	N/A
Multi-year impact:	N/A
Impact included in FES:	N/A
Description of issue:	AG has communicated plans to reconsider (reduce) audit materiality in light of release of unaudited results for 2015/16, and path to balance.
Current status:	OPCD communicating increased AG scrutiny to Ministries in update to FCC, FBMC.
Options under consideration:	No changes to OPCD public accounts process. OPCD collaborating with OPG to gather support for alternative approach in assessing impact of OPG's alternative estimation process for SUDs.
Timing of expected resolution:	February, 2017 in time to be considered for OAG's draft Audit Planning Report
Province's ability to influence:	No certainty regarding AG's acceptance of OPCD's position regarding calculation of SUDs error for OPG's estimated IFRS/US GAAP impact
Role of other ministries:	Ministry of Energy and OFA key stakeholders in matters related to OPG and H1 IFRS analysis MOECC on contaminated sites, GIF, Cap and Trade MOF (ISPPD and ERD) key stakeholders in matters related to Pension Asset Accounting

10. Earlier Release of Public Accounts

Risk:	Medium
Impact in 2016-17 (billions):	N/A
Multi-year impact:	N/A
Impact included in FES:	N/A
Description of issue:	Potentially earlier release date (end of July/16)
Current status:	Assessment underway on key tasks/milestones to deliver by end of July
Options under consideration:	1. Deliver Annual Report and Volumes by end of July 2. Deliver Annual Report only by end of July, to be followed by Volumes in August/September. 3. Impact on Data visualization and open data 4. Process enhancements – in OPCD as well as OAG (needed to complete audit in time to support earlier release, especially in regards to tax estimation.
Timing of expected resolution:	Mid-January
Province's ability to influence:	Dependent on AG's ability to complete her audit and provide copy of audit opinion,
Role of other ministries:	MOF/TBS

Risks: Earlier release date is at the discretion of the Province. Key risk is the tax revenue estimate for which CRA data is only available at the end of July.

11. Implementation of Hyperion Financial Management

Risk:	Medium
Impact in 2016-17 (billions):	N/A
Multi-year impact:	N/A
Impact included in FES:	N/A
Description of issue:	Implementation of Corporate Hyperion Information Reporting Portal in parallel with early release of Public Accounts.
Current status:	CHIRP related considerations integral to discussions on early release date.
Options under consideration:	(Originally planned to rely on CHIRP for 16/17 Public Accounts. Implementation strategy revised pending early release of Public Accounts.
Timing of expected resolution:	N/A
Province's ability to influence:	N/A
Role of other ministries:	OAG to audit controls during 2016/17 public accounts audit. Line and sector ministries to learn how to bet use new system.

Risks: Audit risks to be minimized by relying on legacy systems for 2016/17 Public Accounts. Resource requirements of APFR staff will be high during planned parallel run in addition to earlier planned release for the Public Accounts. Unanticipated audit issues as experienced in 2016 will cause further stress on resources required for the parallel run as well as Public Accounts related processes.

12. Implementation of New Standards

Risk:	Medium/Low
Impact in 2016-17 (billions):	N/A
Multi-year impact:	N/A
Impact included in FES:	N/A
Description of issue:	New standard on related parties and contractual rights to be implemented in 2017/18 requiring planning to ensure that appropriate data available for disclosure.
Current status:	OPCD engagement with OAG on-going to ensure key questions discussed and implementation guidance robust.
Options under consideration:	(XX
Timing of expected resolution:	February, 2017
Province's ability to influence:	Unique to each Province, depending on relative interpretations of PSAB.
Role of other ministries:	TBS – OIAD LSB – restrictions on disclosure for RPT and contractual rights.

Risks: No fiscal impact associated with new standards; however, various stakeholders will have to be involved to ensure completeness and integrity of information required for disclosure. Process will be subject to review by the OAG.