The Regional Municipality of York

Audit Committee
Finance and Administration
June 5, 2019

Report of the Commissioner of Finance

2018 Financial Statements and Auditor's Report

1. Recommendations

Council receive this report for information.

2. Summary

This report provides information to Council on the 2018 financial activities of the Region, as required by the Municipal Act, 2001.

The consolidated financial statements include the financial activities of the Region and all entities that are accountable to and controlled by the Region, including York Region Police Services Board, Housing York Inc., the York Region Rapid Transit Corporation, and YTN Telecom Network Inc.

The audit opinion on the 2018 financial statements was issued without reservation or condition

KPMG LLP conducted the annual financial statement audit in accordance with generally accepted auditing standards. The 2018 Auditor's Report reflects KPMG's opinion that the financial statements present fairly, in all material respects, the financial position of the Region in accordance with generally accepted accounting principles.

The Region's financial picture continues to improve

The Region ended the year with an accumulated surplus; the amount assets exceed liabilities, of $7,219.3 million. The Region's debt, excluding borrowings on behalf of local municipalities and net of sinking fund assets, fell by $170.0 million at year-end and investments rose by $518.2 million, or 18.4% over 2017.

The Region had an annual surplus of $519.7 million

The $519.7 million annual surplus reported in the 2018 consolidated financial statements is the excess of revenues over expenses on a full accrual basis of accounting. In comparison, the Region reported an operating surplus of $35.5 million, which represents the unspent amounts from the operating budget. It is prepared on a modified accrual basis of accounting.

Differences between the two bases of accounting are explained further in this report.

3. Background

Municipalities are required to prepare financial statements and report them to Council

Under the Municipal Act, 2001, municipalities must:

1. Prepare financial statements in accordance with generally accepted accounting principles
2. Report the financial affairs of the municipality to Council
3. Appoint a licensed auditor who is responsible for auditing the accounts and transactions of the municipality annually and expressing an opinion on the municipality's financial statements

The consolidated financial statements were prepared in accordance with Public Sector Accounting Standards

The consolidated financial statements are presented on a full accrual basis of accounting as required by the PSAB. The original budget, on the other hand, was prepared to balance major cash inflows against major cash outflows, and to determine the property tax levy needed to achieve the balance.

The financial statements are comprised of four statements and explanatory notes:

- Consolidated Statement of Financial Position - Represents the Region's balance sheet, consisting of its assets and liabilities, at a specific point in time.
- Consolidated Statement of Operations - Reports the revenues and expenses for the year and the differences between them. The net difference is either an annual surplus or deficit.
- Consolidated Statement of Change in Net Debt - Reconciles the change in net debt for the current and prior year. Under public sector financial reporting in Canada, "net debt" is defined as the difference between financial assets and liabilities.
- Consolidated Statement of Cash Flows - Outlines sources of cash, shows how they were applied, and explains the resulting change in cash and cash equivalents in fiscal 2018.

- Notes to the Consolidated Financial Statements - An integral part of financial statements where additional information is provided to explain specific items in the statements along with the accounting principles used to prepare them.

To best describe the Region's 2018 financial activities, this report focuses on the Consolidated Statement of Financial Position and the Consolidated Statement of Operations.

The Region received the Government Finance Officers Association (GFOA) Award

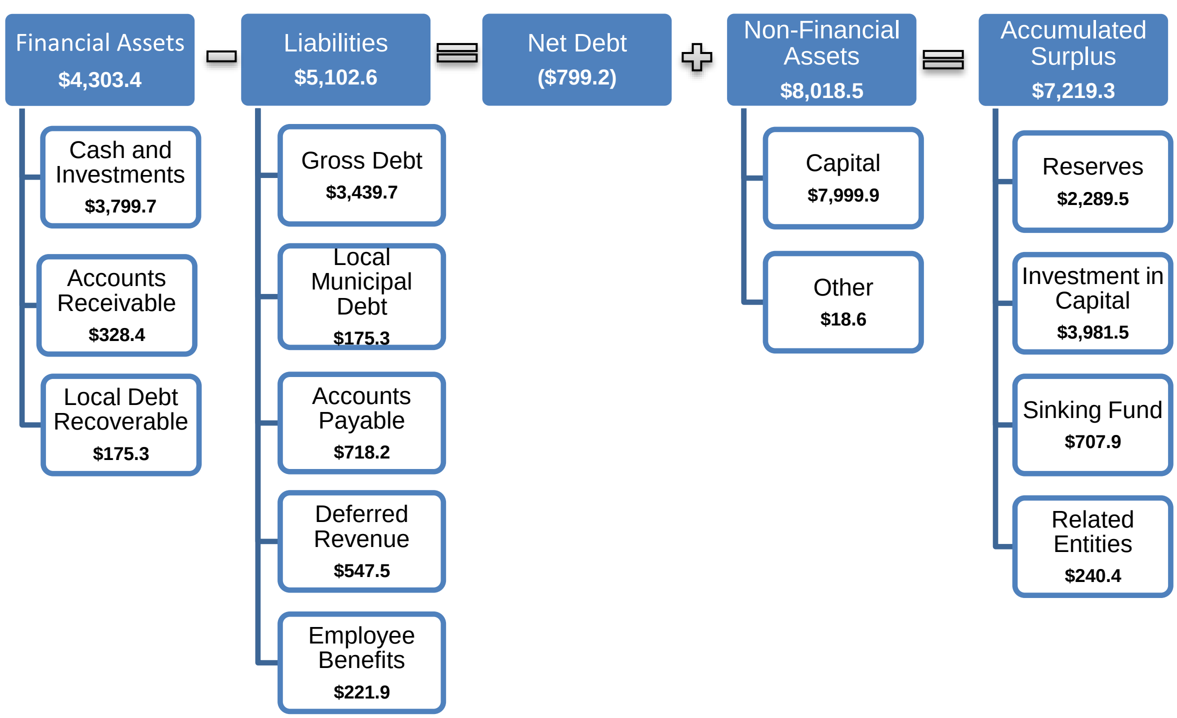
For the twenty-first consecutive year, the Region received the Canadian Award for Financial Reporting from GFOA for its 2017 consolidated financial statements. The award was given for the Region's high quality financial reporting documents that promote accessibility and understandability of financial information. The 2018 financial statements will be submitted for consideration for this award.

4. Analysis

The Consolidated Statement of Financial Position highlights key financial figures

Figure 1 presents the information reported in the Consolidated Statement of Financial Position (in millions).

Figure 1



Financial Assets increased by $455.7 million

Financial assets are assets that can be converted to cash in a short period of time. The Region's financial assets include cash and cash equivalents, investments, accounts receivable from third parties, and debt issued by the Region on behalf of local municipalities.

The largest increase from 2017 relates to investments, which went from $2,809.1 million to $3,327.3 million during the year to reflect the Region's strategy to maximize returns. Investments include resources from reserves and reserve funds that the Region sets up and maintains to cover some of its future spending needs.

Net book value of capital assets increased by $66.6 million

Non-financial assets consist of the Region's tangible capital assets, inventory and prepaid expenses. The Region's non-financial assets increased by $68.7 million or 0.8% from 2017, primarily due to the acquisition and construction of new tangible capital assets during 2018.

The Net Book Value (NBV) is the original cost of the assets less amortization, or estimated usage, since the assets were put into service. The NBV increase of $66.6 million represents additions of $344.1 million less amortization and disposal of assets during the year of $277.5 million.

Figures 2 and 3 present the $7,999.8 million NBV of capital assets by service area and category:

Figure 2

NBV of Tangible Capital Assets by Service Area $(Millions)

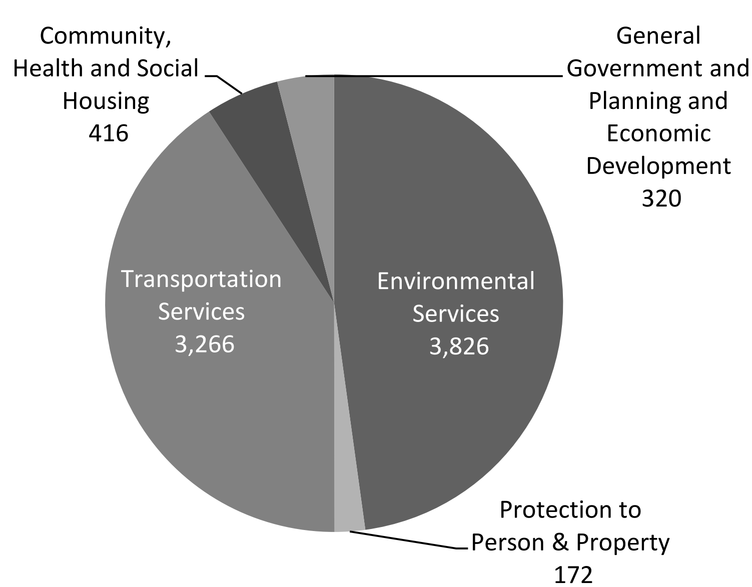
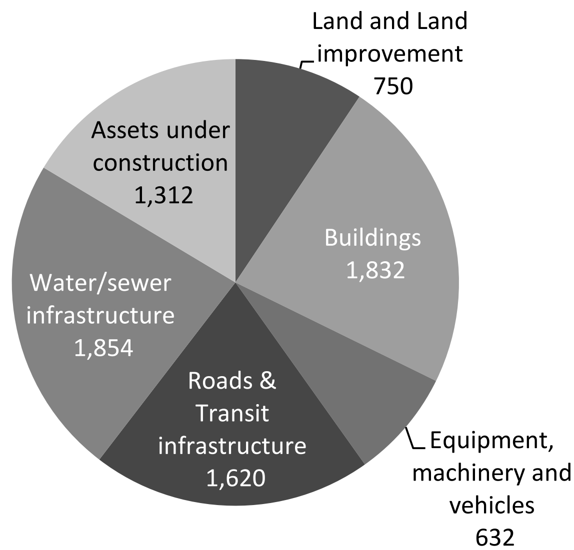


Figure 3

NBV of Tangible Capital Assets by Category $(Millions)



Liabilities increased by $4.8 million

The Region's liabilities consist primarily of long term debt and also include accounts payable, deferred revenue and other obligations.

Total debt as reported in the Consolidated Statement of Financial Position rose by $4.9 million to reach $3,615.0 million at the end of 2018.

This total includes funds borrowed by the Region on behalf of local municipalities. The local municipal borrowings are matched by an asset in the same amount that represents their future debt repayments.

Most of the Region's borrowings are in the form of sinking fund debentures, which require the borrower to set aside funds over time to be used for repayment when the debt matures. The Region's portion of debt, net of sinking fund assets, fell by $170.0 million in 2018, largely reflecting the impacts of the Regional fiscal strategy.

The Region issued $38.8 million in new debt on behalf of local municipalities in 2018.

Liabilities other than long term debt fell by $0.1 million from the previous year.

Net Debt decreased by $451 million from 2017

The Consolidated Statement of Financial Position presents Net Debt as the amount liabilities exceed financial assets. It does not represent the amount of debt owed by the region as discussed above. Rather, net debt provides a measure of the future revenues required by the Region to pay for past transactions and events.

Accumulated Surplus increased by $519.7 million

The accumulated surplus is the total of past annual surpluses and indicates the value of the Region’s net resources, including tangible capital assets, which can be used to provide future services.

The Region ended the year with an accumulated surplus of $7,219.3 million, an increase of $519.7 million, or 7.8% compared to 2017.

The increase in accumulated surplus has been invested in tangible capital assets ($67.7 million) and related entities ($20.5 million), and contributed to reserves and reserve funds ($431.5 million) such as the sinking fund, capital asset replacement and debt reduction reserves.

The financial statements report revenues and expenses on a different basis than the budget

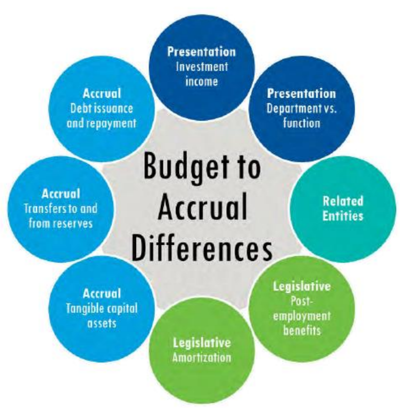
Under full accrual, which is required for government financial reporting, some financial activities are treated differently than in the original budget. In particular, capital spending is not fully expensed at the time an asset is built or acquired. Instead, a portion of the cost is recorded each year in the Consolidated Statement of Operations as amortization. The number of years over which the cost is amortized is based on the expected service life of the asset.

In addition, transfers to and from reserves and the proceeds and repayment of borrowing are not reported as revenue and expenses in the financial statements. As a result, they are removed in the conversion of the original budget to full accrual.

For comparability, the 2018 budget provided an outlook for revenues and expense on a full accrual basis, and the consolidated financial statements compare final results to that outlook.

Figure 4 shows the adjustments required to present the original approved budget on a full accrual basis.

Figure 4



Revenues exceeded expenses in 2018, resulting in an annual surplus of $519.7 million

The Consolidated Statement of Operations reports the Region's revenues and expenses for the year ended December 31, 2018. Revenues exceeded expenses in 2018, resulting in an annual surplus of $519.7 million, an increase of $21.5 million, or 4.3%, compared to 2017. This consists of increased revenue of $250.3 million and an increase in costs of $228.8 million.

Table 1 presents a summary of the Consolidated Statement of Operations. The accrual based budget set out an expected annual surplus of $645.7 million. At $519.7 million, the actual 2018 annual surplus was $126.1 million below budget but $21.5 million higher than the previous year's surplus of $498.2 million.

Table 1

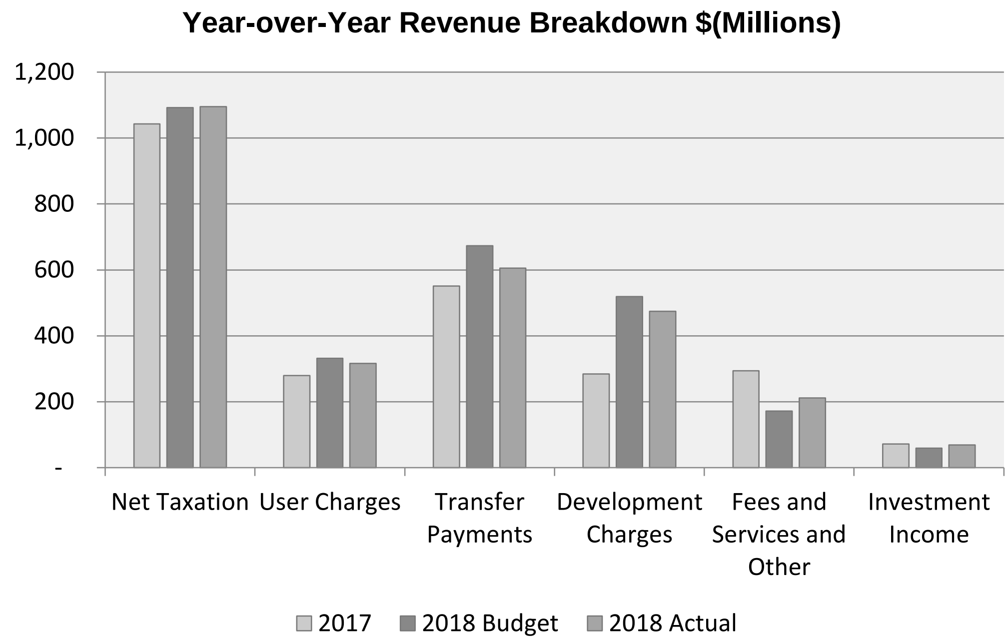
Summary of Consolidated Statement of Operations

$ (Millions)	2018 Budget	2018 Actuals	2017 Actuals	Budget to Actual Variance	Year over Year Variance
Revenue	2,847.9	2,771.3	2,521.0	(76.6)	250.3
Expenses	2,202.2	2,251.6	2,022.8	49.4	228.8
Annual Surplus	645.7	519.7	498.2	(126.0)	21.5

Revenues rose by $250.3 million, reflecting a year-over-year increase of 9.9%

The 2018 budget forecast revenues of $2,847.9 million. Actual 2018 revenues were $76.6 million under budget, at $2,771.3 million. Despite falling short of plan, total revenues grew by $250.3 million from 2017. See Figure 5 below.

Figure 5



The variance in revenues is as follows:

- Net taxation revenues were $2.6 million above budget, at $1,095.1 million, which was in line with the approved tax levy increase of 2.77% and assessment growth of 1.75%.

  This was an increase of $52.5 million or 5.0% from 2017.

- The budget projection for water and wastewater user charges was based on a blended rate increase of 9.0% and expected growth in consumption from 2017, when rainy weather suppressed demand. Actual results were $15.5 million below budget, largely owing to continuing low water flows in 2018.

  Although below budget, this was nonetheless a year over year increase of $37.6 million or 13.5% from exceptionally low 2017 results.

- Revenue from provincial and federal transfers was $67.5 million less than budgeted, at $605.5 million. In 2018, less work than planned was carried out on rapidway projects, which resulted in lower-than-expected revenue from this source.

  Despite coming in lower than budget, transfer payments rose by $54.9 million from 2017 to 2018. Provincial grants totaled $528.6 million, going up in almost all areas. The largest increase was in support for child care, which went from $113.3 million in 2017 to $149.5 million in 2018. Federal funding rose from $61.4 million to $76.9 million, largely reflecting a $19.6 million grant to Environmental Services under the federal Clean Water and Wastewater Fund.

- Development charges, which are revenues from drawing down development charge reserves, were $45.2 million below forecast. This reflected lower-than-expected investments in new growth-related infrastructure, which are funded from this source.

  Although less than forecasted, revenue from development charges drawdowns were $190.5 million, or 67.2%, higher than in 2017.

- Fee and service revenue and other revenue was $39.1 million higher than budgeted. Much of this spending reflects recoveries from local municipalities for capital projects the Region carries out on their behalf. The budget forecast was based on an expected decline in construction activity. The decline was less than expected, so recoveries were higher than planned.

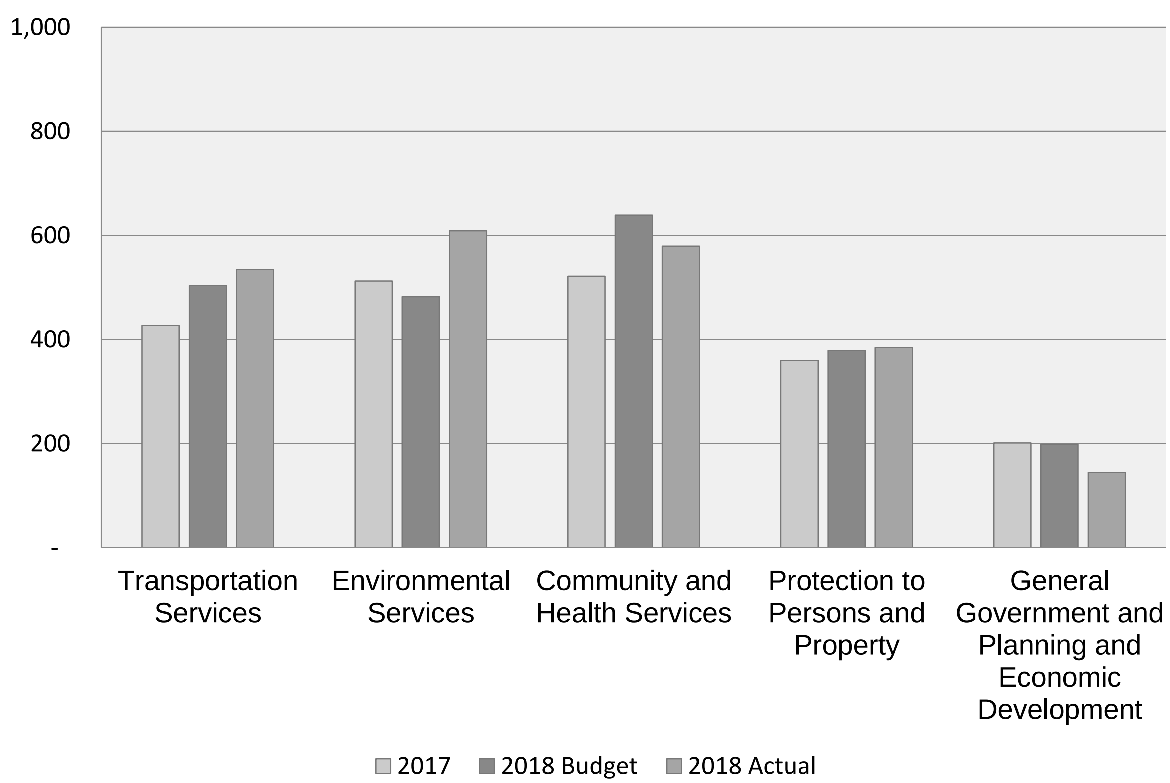
  Nonetheless, the drop in construction activity resulted in a decrease of $82.6 million from 2017.

Expenses grew by $228.8 million, or 11.3% increase compared to 2017

Total operating expenses were $2,251.6 million. This was an increase of $49.4 million from the full accrual budget and $228.8 million from 2017. The increase against the budget resulted mainly from reclassifying a portion of capital spending to expense. On a cash basis, however, the Region did not spend more than outlined in the approved budget. Figure 6 below displays the expense variances on a full accrual basis.

Figure 6

Year-over-Year Expense Breakdown $(Millions)



The largest contributors to the expense variance are:

- In 2018, the Region wrote off over $100.0 million in Environmental capital assets under construction to expense as the amount was recovered from another municipality. This was an accounting adjustment and does not reflect a cash outflow. Apart from that, actual operating costs were close to budget.

  The adjustment also impacted the year over year variance. However, in 2017 there was a similar accounting adjustment in the amount of $55.7 million that reduced the impact on the variance. Apart from these accounting adjustments, operating expense went up in 2018, largely because of the higher regulatory and other costs of operating a larger and more complex water and wastewater system.

- Spending by Transportation Services was $30.5 million above budget, again reflecting an accounting adjustment of roads capital assets under construction to expense as the amount was recovered from other municipalities. This does not reflect a cash outflow. Apart from that change, spending was essentially on budget.

  Transportation Services spending went up by $107.4 million from 2017 to 2018. Apart from the accounting adjustment, this reflected the increased costs to operate and maintain a larger road and transit network, including amortization expense that rose by $15.5 million largely as a result of the subway extension.

- In Community and Health Services, a decrease of $59.5 million from budget was the result of program savings, including lower-than-anticipated payments to support non-profit housing and delays in filling staff vacancies.

  On a year-over-year basis, spending in Community and Health Services rose by $57.5 million, reflecting the increase in transfer payments from the provincial government, particularly for child care programs.

- Spending on Protection to Persons and Property, which largely reflects York Regional Police, was $5.7 million higher than the budgeted amount of $378.8 million, due to a reclassification of employee and post-employment benefit costs (which is discussed further below).

  Spending was up $24.3 million year-over-year as a result of expanded service needs for a growing population and the 2018 reclassification of employee and post-employee benefit costs.

- Spending in the General Government and Planning and Economic Development category was reported at $53.9 million less than budgeted, due mainly to a reclassification in reporting employee and post-employment benefit costs. These costs were previously included in this line, but are now distributed to the appropriate department. The remaining under-spending related to hiring delays and other operating costs that came in lower than budget.

  The change in reporting was the major reason for a decrease of $56.4 million in this item from 2017.

The Region adopted new accounting standards in 2018

The PSAB established five new accounting standards that the Region adopted in its consolidated financial statements in 2018. They are: Contingent Assets; Contractual Rights; Related Party Disclosures; Inter-entity Transactions; and an update to the standard on Assets.

Implementation of these standards had no financial reporting impact on the annual surplus or accumulated surplus and no changes to accounting policies were required. The notes to the financial statements were enhanced as a result of the PSAB required changes to include additional information where necessary.

5. Financial

The Region allocated operating surplus funds totalling $35.5 million to specific reserves

In accordance with the Council-approved reserve and surplus management policy, $35.5 million was allocated from the operating surplus to the reserves and reserve fund accounts. Table 2 shows the surplus allocation.

Table 2
Summary of operating surplus allocation

	$ (millions)
Workers' compensation reserve fund	19.3
Debt reduction reserve fund	13.4
Long term disability reserve fund	1.6
Social housing reserve fund	1.2
	35.5

6. Local Impact

There are no local municipal impacts associated with this report.

7. Conclusion

The 2018 consolidated financial statements reflect the financial results and position of the Region, and are presented in accordance with the Municipal Act, 2001 and Public Sector Accounting Board reporting requirements.

For more information on this report, please contact Jason Li, Acting Director, Controllership Office, Finance Department at 1-877-464-9675 ext. 71683. Accessible formats or communication supports are available upon request.

The Senior Management Group has reviewed this report.

Recommended by:

Laura Mirabella, FCPA, FCA
Commissioner of Finance and Regional Treasurer

Approved for Submission:

Bruce Macgregor
Chief Administrative Officer

May 29, 2019
Attachment (1)
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