City of Spruce Grove

Audit Findings Report
for the year ended December 31, 2019

KPMG LLP

Prepared for the Council meeting on April 27, 2020

kpmg.ca/audit

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Executive summary

Purpose of this report[1]

The purpose of this Audit Findings Report is to assist the Mayor and Council ("Council") in the review of the results of our audit of the consolidated financial statements of the City of Spruce Grove (the "City") as at and for the year ended December 31, 2019. This Audit Findings Report builds on the Audit Plan we presented to Council on November 7, 2019.

Changes from the Audit Plan

Subsequent to December 31, 2019, the COVID-19 outbreak was declared a pandemic by the World Health Organization and has had a significant financial, market and dislocating impact. As such, enhanced subsequent events procedures were warranted.

There have been no other significant changes regarding our Audit Planning Report that was previously presented to you.

Finalizing the Audit

As of April 27, 2020, we have completed the audit of the consolidated financial statements, with the exception of certain remaining procedures, which include:

- Completing our discussions with Council;
- Obtaining evidence of Council's approval of the consolidated financial statements;
- Completing our subsequent events review to the date of Council's approval of the consolidated financial statements; and
- Obtaining a signed management representation letter.

We will update Council on significant matters, if any, arising from the completion of the audit, including the completion of the above procedures. Our auditors' report will be dated upon the completion of any remaining procedures (expected April 27, 2020).

Areas of audit focus

We discussed with you at the start of the audit a number of areas of audit focus:

- Recognition of revenue amounts subject to external restrictions;
- Completeness, existence and accuracy of property assessments and taxation;
- Accuracy and valuation of investments;
- Accuracy and valuation of contributed tangible capital assets;
- Completeness, existence and accuracy of operating costs and accounts payable and accrued liabilities;
- Existence and accuracy of capital expenditures related to approved capital projects;
- Completeness, existence and accuracy of debt;
- Completeness and accuracy of environmental obligations and other contingencies;
- Completeness and accuracy of salaries and benefits note disclosures; and
- Fraud risk from management override of controls.

These matters have been addressed in our audit.

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[1] This Audit Findings Report should not be used for any other purpose or by anyone other than Council. KPMG shall have no responsibility or liability for loss or damages or claims, if any, to or by any third party as this Audit Findings Report has not been prepared for, and is not intended for, and should not be used by, any third party or for any other purpose.

Executive summary (continued)

Significant accounting policies and practices

There is one new accounting standard that has been adopted in the current year: *PSAS3430 Restructuring Transactions*. Note 1(h) to the financial statements describes the adoption of the new accounting standard for the year-ended December 31, 2019.

Note 1(i) to the financial statements describes future accounting standards which may impact the City's reporting in the future.

There were not any other changes to significant accounting policies and practices to bring to your attention.

Critical accounting estimates

Overall, we are satisfied with the reasonability of critical accounting estimates.

Adjustments and differences

Materiality for fiscal 2019 was set at $2,800,000. We identified adjustments that were communicated to management and subsequently corrected in the consolidated financial statements. We identified one difference which remains uncorrected which is not considered to be material and does not impact our audit report on the consolidated financial statements of the City.

We proposed certain adjustments with regards to the City's consolidated financial statement disclosures. The most substantive of these changes were accepted by management and included in the consolidated financial statements.

Control and other observations

We identified one control deficiency that we determined may be of significance to Council.

We have identified other observations we believe may be of interest to Council. None of these deficiencies or observations impact our audit report on the consolidated financial statements of the City.

Additional reporting responsibilities

We have been engaged to report on the following for the year ended December 31, 2019:

- Municipal Financial Information Return (FIR) for the City;
- Local Authorities Pension Plan (LAPP) special reporting;
- APEX special reporting; and
- Family and Community Support Services (FCSS) special reporting.

The consolidated financial statements include the City's proportionate share of the Tri-Municipal Leisure Facility Corporation (a Part 9 Company operating as the TransAlta Tri Leisure Centre) and the Spruce Grove Public Library which are audited by other auditors.

Independence

We are independent with respect to the City, within the meaning of the relevant rules and related interpretations prescribed by the relevant professional bodies in Canada and any other standards or applicable legislation or regulation.

Areas of audit focus and results

We highlight our significant findings in respect of significant financial reporting risks as identified in our discussion with you in the Audit Plan, as well as any additional significant risks identified.

Area of focus	Why are we focusing here?	Our response and significant findings
Recognition of revenue amounts subject to external restrictions	There is a risk of inappropriate revenue recognition of amounts received with external restrictions attached to them (special taxes and levies, government transfers and other amounts).	• We reviewed the recognition of amounts subject to external restrictions, including government transfers and development levies, to ensure they are recognized appropriately. • We confirmed all significant government transfers, and examined related agreements. • We obtained an understanding of the developer levy model and the process the City has in place to recognize revenue related to developer levies. The developer levy model utilizes forecasted development costs, staging and financing requirements to calculate the levy. Changes to these estimated inputs directly impacts deferred development levies and levy revenue. We identified two misstatements relating to prior period offsite levies and government transfers. Refer to the *'Adjustments and differences'* section of the report.
Completeness, existence and accuracy of property assessments and taxation	There is a risk that property assessments and approved tax rates are not applied appropriately.	• We evaluated the application of assessments through the tax roll and taxation rates established by the City. No misstatements or other findings were identified as a result of performing the above procedures.
Accuracy and valuation of investments	There is a risk that investments are not appropriately valued; specifically, impairment of investments is not appropriately assessed and valuation adjustments are not recorded where appropriate.	• We have tested the existence and accuracy of investment accounts through external confirmations, including the cost and market value of investments. • We recalculated investment premiums/discounts for investments recorded at amortized cost. • We have tested management's assessment of impairment and considered if any potential impairment of the investments exists. We provided management with recommendations on the consolidated financial statement disclosures that have been incorporated into the consolidated financial statements. No misstatements or other findings were identified as a result of performing the above procedures.

Areas of audit focus and results (continued)

Area of focus	Why are we focusing here?	Our response and significant findings
Accuracy and valuation of contributed tangible capital assets	There is a risk that contributions of tangible capital assets are not appropriately captured in the consolidated financial statements.	• We obtained an understanding of the process by which departments capture tangible capital assets which are contributed from developers and other parties and assessed the consistency of the process applied across all departments. • We tested a sample of developments which were completed by the City during the year to assess whether the assets have been appropriately recorded. • We reviewed the value ascribed to assets contributed to the City for reasonableness. • We reviewed a sample of developments currently ongoing at the City to ensure they have been appropriately excluded as contributed assets during the year. We identified one misstatement relating to additions that were not captured as part of tangible capital assets. Refer to the *'Adjustments and differences'* section of the report.
Completeness, existence and accuracy of operating costs and accounts payable and accrued liabilities	There is a risk that appropriate cut-off of accounts payable and accrued liabilities is not achieved.	• We used our understanding of the City's operations, our discussions with management and our review of Council minutes to evaluate the completeness of accruals as at December 31, 2019. • We performed work over the City's budgeting process and obtained a detailed understanding of significant variances from the approved budget. • Our year-end procedures included a search for unrecorded liabilities (primarily through a review of unprocessed transactions and payments subsequent to year-end) and a detailed analysis of key accruals. No misstatements or other findings were identified as a result of performing the above procedures.
Existence and accuracy of capital expenditures related to planned capital projects	There is a risk that capital expenditures are not appropriately recorded in the financial statements and are not appropriately recorded related to approved capital projects.	• We reviewed a sample of capital expenditures and ensured they were applied against the appropriate capital projects. No misstatements were identified as a result of performing the above procedure; however, we did note that improvements could be considered to the capital budgeting process of the City. Refer to the *'Control and other observations'* section of this report.

Areas of audit focus and results (continued)

Area of focus	Why are we focusing here?	Our response and significant findings
Completeness, existence and accuracy of debt	There is a risk that there is a breach in compliance with debt and that the debt is not appropriately recorded in the financial statements.	• We used our understanding of the City's operations, discussions with management and review of Council minutes to determine if completeness of debt has been achieved. • We confirmed all significant outstanding debt obligations and other key features of debt, including amounts outstanding at period end, interest rates, debt maturity and repayment terms, restrictive covenants, and assets pledged and guarantees, etc. • We assessed compliance with restrictive covenants for all debt agreements, including debt limit regulation. No misstatements or other findings were identified as a result of performing the above procedures.
Completeness and accuracy of environmental obligations and other contingencies	There is a risk that environmental obligations and other contingent liabilities are not appropriately identified and reasonably estimated.	• We reviewed the City's update of land and other assets for the potential risk of contamination and determination of a resulting obligations, if any. • We are satisfied that the City has procedures in place to ensure consistent and accurate identification of environmental obligations and other contingencies. No misstatements or other findings were identified as a result of performing the above procedures.
Completeness and accuracy of the salaries and benefits note disclosures	There is a risk that salaries and benefits note disclosures are not complete and accurately reported.	• We reviewed a sample of employment contracts to ensure salaries and benefits are appropriately disclosed. No misstatements or other findings were identified as a result of performing the above procedures.
Fraud risk from management override of controls	This is a presumed risk. We have not identified any specific risks relating to this audit.	• We evaluated the design and implementation of controls surrounding journal entries, and tested entries made at the end of the reporting period. We identified a finding related to the initiation and posting of journal entries. Refer to the '*Control and other observations*' section of this report. No misstatements or other findings were identified as a result of performing the above procedures.

Critical accounting estimates

Management is required to disclose information in the consolidated financial statements about the assumptions it makes about the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to carrying amounts of assets and liabilities within the next financial year. Generally, these are considered to be "critical accounting estimates."

We have summarized our assessment of the subjective areas.

Asset / Liability	KPMG Comment
Environmental obligations and other contingencies	The City obtained information from external and internal resources who specialize in assessing potential environmental obligations and other contingencies. There have been no significant changes in how the obligations are estimated year over year.
Useful lives of tangible capital assets	The City estimates the useful life of tangible capital assets and reviews the amortization policy on a regular basis. There have been no changes to the manner in which the estimate is determined.
Accrued liabilities	The City estimates accrued liabilities based on expenses and payables incurred throughout the year. There is no change in the way the City estimates accrued liabilities from the prior year.
Allowance for doubtful accounts receivable	The City estimates allowance for doubtful accounts (taxes and other) based on historical collections and examination of aged balances due over 90 days. There have been no changes in the manner in which this estimate is determined.
Fair value of contributed tangible capital assets	The City typically relies on the value of the contributed tangible capital asset as outlined on tender amounts or historical costing information obtained from developers or other sources and applied to quantities as measured by the planning and development services department using the GIS system. There have been no changes to the manner in which the estimate is determined.
Deferred revenue and revenue recognized related to development charges and levies	The City utilizes forecasted development costs, staging and financing requirements to determine levy rates for development and related amounts to be recognized as revenue. There have been no changes in the manner in which the rates are calculated by the City's development model.

Financial statement presentation and disclosure

The presentation and disclosure of the financial statements are, in all material respects, in accordance with the City's relevant financial reporting framework. Misstatements, including omissions, if any, related to disclosure or presentation items are in the management representation letter.

We also highlight the following:

Form, arrangement, and content of the financial statements	The consolidated financial statements have been prepared in accordance with the Canadian public sector accounting standards. As disclosed in Note 1(h) of the City's consolidated financial statements, a new Canadian public sector accounting standard came into effect for the City's year ending December 31, 2019, PS34390 – Restructuring Transactions. We reviewed the City's assessment regarding the new standard and concur with management's conclusion that the adoption of this accounting standard did not result in any changes to the measurement or disclosures in the consolidated financial statements.
Application of accounting pronouncements issued but not yet effective	As described in Note 1(i) of the City's consolidated financial statements, a number of new Canadian public sector accounting standards will be in effect beginning with the City's December 31, 2021 year end and beyond. These new standards include: PS1201 – Financial Statement Presentation; PS2601 – Foreign Currency Transactions; PS3041 – Portfolio Investments; PS3450 – Financial Instruments; PS3280 – Asset Retirement Obligations; and PS3400 – Revenue. Although it is not anticipated these new accounting standards will result in significant measurement differences in the City's consolidated financial statements in future years, additional disclosures will likely need to be provided.

Adjustments and differences

Differences and adjustments include disclosure differences and adjustments.

Professional standards require that we request of management and Council that all identified differences be corrected. We have already made this request of management.

Corrected adjustments

The management representation letter includes all adjustments identified as a result of the audit, communicated to management and subsequently corrected in the financial statements.

Further, we proposed certain adjustments with regards to the City's consolidated financial statement disclosures. The most substantive of these changes were accepted by management and included in the consolidated financial statements.

Adjustments and differences (continued)

Uncorrected differences

Based on both qualitative and quantitative considerations, management has represented to us that the differences —individually and in the aggregate—are, in their judgment, not material to the financial statements. We concur with management's representation that the differences are not material to the financial statements. Accordingly, the differences have no effect on our auditors' report.

As at December 31, 2019	Annual Surplus Increase (Decrease)	Financial position Increase (Decrease)		
Description of differences greater than $139,000 individually		**Assets**	**Liabilities**	**Opening Accumulated Surplus**
Materiality - $2,800,000				
To record the uncorrected misstatement for the overstatement of developer contributions and levies for revenues related to prior years that was adjusted in the current year.	$ (1,472,000)	–	–	$ 1,472,000
Total differences	**$ (1,472,000)**	**–**	**–**	**$ 1,472,000**

Control and other observations

We have highlighted the matters below that we would like to bring to your attention:

Item	Observations and Recommendations (2017 and 2018)	2019 Update
Capital budgeting, including budgeting for contributed tangible capital assets	**Observation:** We noted that the budgeted amount for the acquisition of tangible capital assets does not reflect actual acquisitions for the year. This is because the capital budget is based on projects approved which may span multiple years instead of planned cash flow for the year including carry forward amounts from prior years. We acknowledged that the City has controls in place to monitor the progress of capital projects in progress and that these results are reported to Council on a regular basis. However, this underlying understanding of the timing of capital projects does not translate to the capital budget approved by Council and the amounts that are ultimately reported within the consolidated financial statements of the City. Capital budget processes that are not fully integrated with internal and external financial reporting expose the City to potential operational, taxation, investing and financing implications. **Recommendation:** We recommended that the City review the components of its capital plan. These components include its processes for capital budget amendments, its historic capital priorities including approved but delayed capital projects, and the carryforward amounts that are brought forward into the upcoming fiscal year to ensure the City has the capacity and funds necessary to execute and complete the capital projects.	In 2019, we noted that the budgeted acquisition of tangible capital asset compared to the actual acquisition of tangible capital assets resulted in an approximately $12.5 million variance on the consolidated financial statements which represents and improvement over prior years. As the City is still in the process of reviewing its budgeting processes, we will follow up on the final implementation of this recommendation in 2020.

Control and other observations (continued)

Item	Observations and Recommendations (2017 and 2018)	2019 Update
Alignment of internal and external financial reporting	**Observation:** Although the City is not required to prepare an overall annual report, the majority of municipalities do so which includes an overview of their annual operational results and achievements, key performance indicators (KPIs) and metrics, as well as audited financial statements. Annual reports provide a reporting mechanism for a municipality to communicate qualitative and quantitative results, both annually and on a longer term basis. We note that the City does include summary financial information in its City*pulse* publication. In addition to City*pulse*, and as per Council direction, Administration is developing KPIs for the City and is assessing how such measures might be tracked and communicated both internally and externally. Furthermore, the City has begun reporting quarterly non-consolidated financial results on its external website through a tool called *Open Books*, which is designed to make the City's financial reporting more accessible to the public. **Recommendation:** We recommended that management consider preparing a more comprehensive annual report for its citizens and shareholders. An annual report is a fully integrated report, and therefore, is a City-wide initiative, requiring data and analysis from many relevant places. We understand that the City continues to maintain and track such relevant data, however the coordination of data for an annual report has not yet occurred. As Administration considers an integrated reporting mechanism, it should ensure that the annual report is consistent with its internal and external financial statements, and that relevant KPIs and other metrics are presented.	In the current year, we noted no inconsistencies with the *Open Books* platform used by management. However, although this is an improvement to the City's external reporting, the platform does not present relevant KPIs and other metrics, items that should be included in an annual report. We will continue to follow-up on this matter as part of the 2020 audit process.

Control and other observations (continued)

Item	Observations and Recommendations (2017 and 2018)	2019 Update
Completeness/Accuracy of the City's budget preparation workbooks	**Observation:** We noted unusual variances when comparing current year budgeted to actual figures for utilities and sales and user fees. It was determined that these operating budget variances were a result of formula errors in the City's workbook used to prepare the 2017 budget. We further noted that there were differences in the 2018 consolidated budget figures due to unposted elimination entries for related party transactions with the Tri-Leisure Centre and Spruce Grove Public Library. It was determined that the City does not prepared a consolidated budget reconciliation to identify unusual differences. **Recommendation:** We recommended that the City enhance its review processes with respect to its budget workbooks to ensure there are no formula or other errors in the preparation of future operating budgets and also perform a consolidated budget reconciliation.	In the current year, we noted that management remediated the formula errors identified in 2018 and also performed a consolidated budget reconciliation to enhance its review process. However, we noted differences between the re-calculated consolidated budget figures and the amounts presented within the consolidated financial statements. It was identified that two accounts were excluded from the budget calculation. Management has corrected this discrepancy in the consolidated financial statements. As such, our recommendation for the City to continue to enhance its review processes remain. We will continue to follow-up on this matter as part of the 2020 audit process.

Control and other observations (continued)

Item	Observations and Recommendations (2017 and 2018)	2019 Update
Implementation of an asset management system that is integrated with the City's financial reporting	**Observation:** During our audit of the City's tangible capital assets (TCAs), we identified the following matters: • Currently, the City does not maintain an integrated asset management system that integrates to the City's financial records and internal and external reporting. The City records and tracks TCAs manually, using a series of excel spreadsheets which are susceptible to error; • Certain contributed TCAs from prior years were not identified in the City's financial records; however, knowledge of these contributes TCAs existed within the City's engineers; • There is no formal review of work in progress TCAs at year end to ensure any completed TCAs that are in use are appropriated transferred to the correct asset class on a timely basis; and • There is no formal reconciliation of land recorded in the City records to Alberta Land Titles. In 2018, we noted improvements in reconciling land recorded in the City records to Alberta Land Titles, such that management has implemented a formal reconciliation process. However, it was noted that this process took place at a time prior to year-end and there was a lack of formal process to reconcile land for the remaining period to year end. **Recommendation:** An integrated asset management system would improve City processes by reducing the likelihood of manual errors and reducing the communication gap and burden between Finance and other City departments. We also recommend that management continue to improve this process by performing the initial reconciliation after the typical "construction season" and developing a process to ensure completeness and accuracy of land recorded in the City records for the remaining portion of the year.	Consistent with prior years, we understand that the City intends to implement an integrated asset management system and will transition various asset classes to the new system over time. We are supportive of this transition and recommend that management continue with integrating this system. In the current year, we noted improvements to the formal reconciliation process of reconciling City records to Alberta Land Titles. A formal process was in place and no errors resulted in the reconciliation. We will continue to follow-up on the integration of the system as part of the 2020 audit process.

Control and other observations (continued)

Item	Observations and Recommendations (2017 and 2018)	2019 Update
Operating segments presentation and disclosure	**Observation:** The City's consolidated financial statements are prepared in accordance with Public Sector Accounting Standards (PSAS), which includes the requirement to report segments. PSAS defines segments as a distinguishable activity or group of activities of a government for which it is appropriate to separately report financial information. The determination of segments required the application of professional judgment as there are not prescribed segments. While PSAS has a list of factors to consider, a starting point for segments could be the major classifications of activities that are used in creating, presenting, or managing budget information. Managing segments in this manner reflects the existing accountability framework for government and the way operations are managed. In 2017 and 2018, the City reported its operating segments as Municipal, Utility and Development. These segments do not provide meaningful information as intended, as they do not appear to align directly to the City's budget, or how they manage City operations. **Recommendation:** We recommended that the City review its segment disclosures with the intent of aligning the reported segments to how the City manages and reports its operations. Once meaningful segments are identified, these segments should be reported consistently throughout the consolidated financial statements and any related internal and external financial information that is reported.	In the current year, we noted that the segmented disclosures in Note 14 were aligned with how the City manages and reports its operations (i.e. separated through General Government, Protective Services, etc.). This provides meaningful information that align with the City's operations. We consider this matter resolved and it will be removed from future reporting.

Control and other observations (continued)

Item	Observations and Recommendations (2018)	2019 Update
Journal entry control	**Observation:** During our audit of the City's journal entry process, we noted a lack of preventative system controls in place to ensure that all journal entries posted into the accounting system have been approved by an appropriate individual, or that the initiation and posting of journal entries is appropriately segregated between individuals. Further, the City currently does not have a manual review process whereby journal entries are required to be reviewed prior to the entries being posted. The City has an alternative process in place whereby the financial team prepares a detailed variance analysis of financial results on a monthly basis that would identify any significant inappropriate journal entries. This control is considered to be a mitigating control. The potential implications from a lack of appropriate preventative controls can be pervasive such that inappropriate journal entries may go undetected. During our audit work, no misstatements or other inappropriate journal entries were identified. **Recommendation:** We understand that the City is currently in the process of updating and revising internal policies and processes. As part of this activity, we recommend that the City review its current journal entry review process to identify and remediate areas where a lack of segregation of duties may be present, as well as investigate system controls that can be implemented to require approval of journal entry by an appropriate individual prior to posting.	During the current year, we did not identify any changes to this process, however no misstatements or other inappropriate journal entries were identified. The City is planning to reform all policies in the 2020 year, with the journal entry process being part of this reform. As such, our recommendation still remains in regards to this process. We will continue to follow-up on this matter as part of the 2020 audit process.

Control and other observations (continued)

Item	Observations and Recommendations (2018)	2019 Update
Policy updates	**Observation:** During our audit, we obtained an understanding of the City's suite of financial and non-financial policies, and compared to policies that would be expected. Through these procedures, we noted various policies that had not been updated in a number of years and as a result, were lacking key pieces of information that should be considered in order to provide appropriate strategic direction to management. **Recommendation:** We understand that the City is currently in the process of updating and revising certain internal policies and processes. We are supportive of this transition, and enhancement to processes and quality of information. We recommend that while updating and revising internal policies and process, we encourage the City to consider appropriate segregation of duties in all financial processes (i.e. journal entries, purchasing & receiving, etc.) as well as implementing formal Conflict of Interest policies and procedures.	During the current year, we did not identify any changes to the internal policies and processes, The City is planning to reform all policies in the 2020 year, with the journal entry process being part of this reform. As such, our recommendation still remains. We will continue to follow-up on this matter as part of the 2020 audit process.

Audit response to COVID-19 Pandemic

Subsequent events

Subsequent to December 31, 2019, the COVID-19 outbreak was declared a pandemic by the World Health Organization and has had a significant financial, market and social dislocating impact.
As such enhanced subsequent events procedures are warranted.

Our audit approach

There are two types of subsequent events, with the accounting treatment dependent on the categorization as follows:

- Events that provide future evidence of conditions that existed at the financial statement date. For these conditions, the financial statements should be adjusted for measurable impact to the assets, liabilities, revenues and expenditures.
- Events that are indicative of conditions that rose subsequent to the financial statement date. For these conditions, disclosures, at a minimum, should include a description of the event and an estimate of the financial impact, when practicable or a statement that an estimate cannot be made.

Audit response

- Management should work with the audit team to customize language for a subsequent events note.
- An assessment for any financial indicators of financial implications should be undertaken and documented by management.
- A list of any financial implications and actions undertaken by the entity should be disclosed in the notes, examples may include:
  - Experienced temporary declines in the fair value of investments and investment income
  - Closure of facilities to the date of the auditors' report based on public health recommendations to slow the transmission
  - Temporary and or permanent termination of employees
  - Mandatory working from home requirements for those able to do so
  - Others as appropriate
- A statement as to whether or not these factors present uncertainty over future cash flows, may cause significant changes to the assets or liabilities and may have a significant impact on future operations. Along with measurement of an estimated impact on the financial effect or indication if one is not practicable at this time.

Management has included a subsequent events note in its financial statements that appropriately describes and responds to the above matter.

Resources for Management Finance and Audit committee members

Please visit our COVID-19 website for resources. This site is being updated daily based on information being released by Federal, Provincial and Municipal news releases. *https://home.kpmg/ca/en/home/insights/2020/03/the-business-implications-of-coronavirus.html*

Appendices

Appendix 1: Other Required Communications

In accordance with professional standards, there are a number of communications that are required during the course of and upon completion of our audit. These include:

Auditors’ report	Management representation letter
The conclusion of our audit is set out in our draft auditors’ report as attached.	In accordance with professional standards, a copy of the management representation letter are provided to Council. The management representation letter is attached.

Audit quality

Audit Quality (AQ) is at the core of everything we do at KPMG. Appendix 2 provides more information on AQ.

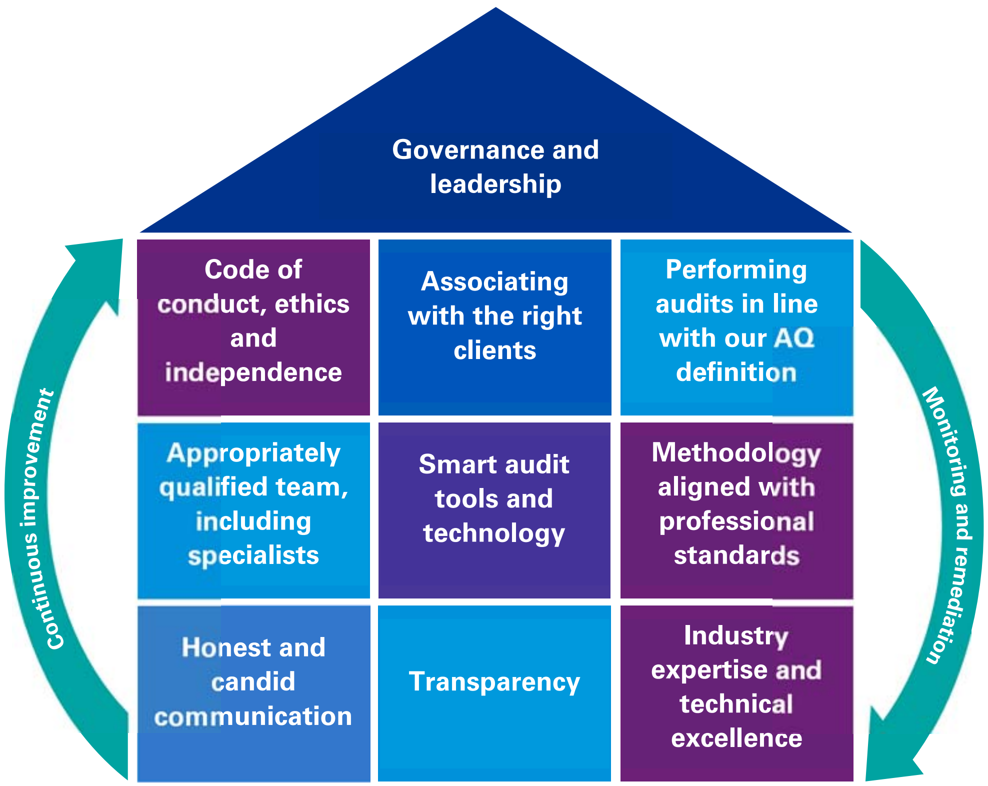
The following links are external audit quality reports for reference:

- CPAB Audit Quality Insights Report (October 2019) (formerly the “Big Four Firm Public Report”)
- Auditing in the Crypto-Asset Sector: 2019 Inspections Insights (Nov 2019)

Appendix 2: Audit Quality and Risk Management

KPMG maintains a system of quality control designed to reflect our drive and determination to deliver independent, unbiased advice and opinions, and also meet the requirements of Canadian professional standards.

Quality control is fundamental to our business and is the responsibility of every partner and employee. The following diagram summarizes the key elements of our quality control system.



Audit Quality Framework

What do we mean by audit quality?

Audit Quality (AQ) is at the core of everything we do at KPMG.

We believe that it is not just about reaching the right opinion, but how we reach that opinion.

We define 'audit quality' as being the outcome when audits are:

- Executed consistently, in line with the requirements and intent of applicable professional standards within a strong system of quality controls and
- All of our related activities are undertaken in an environment of the utmost level of **objectivity, independence, ethics,** and **integrity**.

Our AQ Framework summarises how we deliver AQ. Visit our Audit Quality Resources page for more information including access to our Audit Quality and Transparency report.

Appendix 3: Preparing for PSAB Standard Changes

KPMG

Preparing for PSAB Standard Changes

Are you ready to implement PSAB's impactful series of new standards?

Public sector entities are preparing to implement three significant Public Sector Accounting standards through 2022. These standards will impact not only your accounting policies, but also how Finance engages key stakeholders.

Asset Retirement Obligations

PS3280 addresses the reporting of legal obligations associated with the retirement of certain tangible capital assets and solid waste landfill sites by public sector entities.

PS3280 will apply to fiscal years beginning on or after April 1, 2021. Earlier adoption is permitted. Three transition options are available – retroactive, modified retroactive, prospective.

Asset retirement activities are defined to include all activities related to an asset retirement obligation. These may include but are not limited to:

- decommissioning or dismantling a tangible capital asset that was acquired, constructed or developed
- decontamination created by the normal use of the tangible capital asset
- post-retirement activities such as monitoring
- constructing other tangible capital assets in order to perform postretirement activities

With the introduction of PS3280 PSAB has withdrawn existing Section PS3270, solid waste landfill closure and post-closure liability.

Some examples of asset retirement obligations which fall under scope of proposed PS3280 include:

- end of lease provisions (from a lessee perspective)
- removal of radiologically contaminated medical equipment
- wastewater or sewage treatment facilities
- firewater holding tanks
- closure and post-closure obligations associated with landfills
- septic beds
- fuel storage tank removal

Under PS3280, an asset retirement obligation should be recognized when, as at the financial reporting date, ALL of the following criteria are met:

- there is a legal obligation to incur retirement costs in relation to a tangible capital asset
- the past transaction or event giving rise to the liability has occurred
- it is expected that future economic benefits will be given up
- a reasonable estimate of the amount can be made

Whether you are an education or health institution or a government entity (federal, provincial, municipal or Indigenous) this accounting standard will have implications for your organization if you report under the Public Sector Accounting Standards.

Are You Ready?

1. *Has a project plan been developed for the implementation of this section?*
2. *Has Finance communicated with key stakeholders, including Council or Board on the impact of this section?*
3. *Does Finance communicate with representatives of the Public Works, Asset Management, Facilities Management or Legal functions through the financial reporting process?*
4. *Has a complete inventory been developed of all inactive or active assets or sites, to provide a baseline for scoping of potential retirement obligations?*
5. *If a complete inventory has been developed, does it reconcile back to information currently reported in the entity's financial statements for tangible capital assets or contaminated sites?*
6. *Does your entity have data on non-recorded assets or sites (ie: assets which were originally expensed on purchase, or recorded at no book value) which could have retirement obligations?*
7. *Does your entity have an active solid waste landfill site?*
8. *If yes, does your entity have an existing estimate of the full costs to retire and monitor the landfill site?*
9. *Is your entity aware of any of its buildings which have asbestos?*
10. *If so, does your entity have information to inform a cost estimate to remove/ treat the asbestos?*
11. *Is your entity aware of underground fuel storage tanks or boilers which must be removed at end of life?*
12. *If so, does your entity have information to inform a cost estimate to remove the tanks?*
13. *Is your entity aware of any lease arrangements where it will be required to incur costs to return the premises to pre-existing conditions at the end of the lease?*
14. *Has your entity determined if it has any sewage or wastewater treatment plants which have closure plans or environmental approvals which require full or partial retirement of the plant at the end of its life?*
15. *Is your entity aware of any other contractual or legal obligations to retire or otherwise dismantle or remove an asset at the end of its life?*

Revenues

PS3400 outlines a framework describing two categories of revenue – transactions with performance obligations (exchange transactions) and transactions without performance obligations (unilateral transactions).

- This section will apply to fiscal years beginning on or after April 1, 2022, with earlier adoption permitted.
- This Section may be applied retroactively or prospectively.
- This section will not impact the present accounting for taxation revenues and government transfers.

Transactions which give rise to one or more performance obligations are considered to be exchange transactions. Performance obligations are defined as enforceable promises to provide goods or services to a payer as a result of exchange transactions. Revenue from an exchange transaction would be recognized when the public sector entity has satisfied the performance obligation(s), at a point in time or over a period of time.

If no performance obligations are present, the transaction would represent unilateral revenue, and be recognized when the public sector entity has the authority to claim or retain an inflow of economic resources and a past event gives rise to a claim of economic resources.

Public sector entities will need to review their revenue recognition policies for in-scope transaction types. Impacted areas may include:

- Development charges
- Permits
- Licences
- Advertising programs

Are You Ready?

1. *Has the entity identified any revenue-generating transactions other than taxation or government transfer revenues which create performance obligations (ie: the entity is required to provide a good or service to earn that revenue)?*
2. *If so, has the entity reviewed its accounting policies for these transactions to verify revenue is recognized only as performance obligations are being met?*
3. *Has the entity quantified the impact of any change in accounting policy, or determined that there is no impact?*

Financial Instruments

PS3450 establishes standards on how to account for and report all types of financial instruments including derivatives.

- This Section applies to fiscal years beginning on or after April 1, 2021. Earlier adoption is permitted.
- Government organizations that applied the CPA Canada Handbook – Accounting prior to their adoption of the CPA Canada Public Sector Accounting Handbook applied this Section to fiscal years beginning on or after April 1, 2012.
- This section must be adopted with Section PS 2601, Foreign Currency Transaltion.
- Specific transition requirements are outlined in the section.

This section prescribes a fair value measurement framework for derivatives, and equity instruments that are quoted in an active market.

Where an entity manages risks, the investment strategy, or performance of a group of financial assets, financial liabilities or both on a fair value basis, they may also be meased at fair value.

Other financial instruments are measured at cost/ amortized cost.

Changes in the fair value of a financial instrument in the fair value category are recognized in the Statement of Remeasurement Gains and Losses as a remeasurement gain or loss until the financial instrument is derecognized.

- Upon derecognition, the remeasurement gain or loss is realized in the Statement of Operations.

Are You Ready?

1. *Does the entity hold any financial assets which are equity or derivative instruments?*
2. *Has the entity determined if it has any embedded derivatives that might arise from existing contractual arrangements?*
3. *Does the entity have other financial assets which it assesses performance of based on fair value, and for which it might elect a fair value measure?*
4. *If yes to any of the above three questions, does the entity have readily observable market data to inform a fair value measure?*
5. *Has the entity reviewed existing financial instrument note disclosure in the financial statements to determine any required revisions to meet the requirements of this section?*
6. *Does the entity enter into transactions involving foreign exchange?*
7. *Does the entity hold any monetary assets and monetary liabilities, or non-monetary assets denominated in a foreign currency?*

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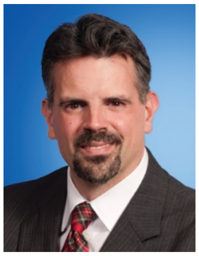

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