

APPENDIX A

CITY OF NANAIMO, BRITISH COLUMBIA, CANADA FINANCIAL REPORT

for the year ended December 31, 2017

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CITY OF NANAIMO MANAGEMENT REPORT

For the Year Ended December 31, 2017

The Council of the City of Nanaimo has delegated the responsibility for the integrity and objectivity of the financial information contained in the financial statements to the management of the City of Nanaimo. The financial statements which, in part, are based on informed judgments and estimates, have been prepared by management in accordance with Canadian public sector accounting standards, which have been applied on a basis consistent with that of the preceding year.

To assist in carrying out their responsibility, management maintains an accounting system and internal controls to provide reasonable assurance that transactions are properly authorized and recorded in compliance with legislative and regulatory requirements and that financial records are reliable for preparation of financial statements. These systems are monitored and evaluated by management.

The City of Nanaimo's independent auditors, KPMG LLP, are engaged to express an opinion as to whether these financial statements present fairly the City of Nanaimo's financial position and operating results in accordance with Canadian public sector accounting standards. Their opinion is based on procedures they consider sufficient to support such an opinion.

The financial statements have, in management's opinion, been properly prepared within reasonable limits of materiality and in accordance with Canadian public sector accounting standards. These statements present, in all significant respects, the financial position of the City of Nanaimo as at December 31, 2017.

Sheila Gurrie
Corporate Officer

Laura Mercer, CPA, CGA
Deputy Financial Officer

Auditors' Report

To the Shareholders
City of Nanaimo

This is a placeholder.

City of Nanaimo

CITY OF NANAIMO
CONSOLIDATED STATEMENT OF FINANCIAL POSITION

as at December 31, 2017, with comparative figures for 2016

	2017	2016
FINANCIAL ASSETS		
Cash and cash equivalents	\$ 51,082,470	\$ 69,589,008
Accounts receivable (Note 2)	20,190,612	15,712,240
Development cost charges receivable (Note 3)	563,650	312,517
Temporary investments (Note 4)	140,151,672	112,666,810
	211,988,404	198,280,575
LIABILITIES		
Accounts payable and accrued liabilities (Note 5)	29,881,200	31,198,247
Compensated absences and termination benefits (Note 6)	7,364,676	6,989,480
Deferred revenue (Note 7)	17,210,247	16,980,784
Deferred development cost charges (Note 8)	42,617,685	42,228,902
Debt (Note 9)	42,335,511	43,925,300
	139,409,319	141,322,713
NET FINANCIAL ASSETS	72,579,085	56,957,862
NON-FINANCIAL ASSETS		
Tangible capital assets (Note 10)	686,215,676	681,128,718
Prepaid expenses	1,213,866	1,185,506
Inventories of supplies	1,062,170	818,664
	688,491,712	683,132,888
ACCUMULATED SURPLUS (Note 11)	\$ 761,070,797	\$ 740,090,750

Commitments and contingencies (Note 12)

Approved on behalf of the Council

William B. McKay
Mayor

Bill Bestwick
Councillor, Chair Finance & Audit Committee

CITY OF NANAIMO CONSOLIDATED STATEMENT OF OPERATIONS

for the year ended December 31, 2017, with comparative figures for 2016

	2017 Budget (Note 14)	2017	2016
REVENUES			
Taxes	\$ 101,610,817	\$ 101,772,627	\$ 98,006,106
Payments in lieu of taxes	1,795,482	1,858,365	1,459,260
Taxation and payments in lieu (Note 15)	103,406,299	103,630,992	99,465,366
User fees and sales of services (Note 16)	38,242,851	39,794,704	38,348,292
Other revenue	4,914,262	6,511,918	5,881,915
Development cost charges (Note 8)	10,772,486	6,802,341	5,390,435
Transfers from other governments-operating (Note 17)	4,173,312	4,629,890	4,331,607
Transfers from other governments-capital (Note 17)	7,283,481	3,745,004	3,679,418
Developer assets received (Note 10)	-	3,724,488	8,126,066
Investment income	2,784,053	3,403,150	3,010,006
Building permits	1,250,000	1,885,202	1,619,320
Regional recreation sharing	1,113,566	1,113,566	1,091,640
Donations and contributions-capital	4,136,953	972,902	1,018,653
Property rentals	961,438	961,546	1,021,916
Municipal Finance Authority refunds and debt forgiven	-	-	4,449
	179,038,701	177,175,703	172,989,083
EXPENSES			
Police	28,576,553	28,580,462	29,399,255
Parks and recreation	27,991,375	27,838,680	25,581,174
Engineering and public works	27,427,521	27,046,043	25,933,296
Fire	17,685,195	17,458,206	16,915,612
Waterworks	16,285,726	14,600,044	14,312,684
Corporate services	14,387,864	12,328,650	12,485,893
Development services	12,305,401	11,023,615	11,776,206
City administration	9,043,194	8,683,228	7,866,458
Sewer System	5,560,959	4,755,490	4,751,084
Port of Nanaimo Centre	4,900,072	3,881,238	5,507,047
	164,163,860	156,195,656	154,528,709
ANNUAL SURPLUS	14,874,841	20,980,047	18,460,374
ACCUMULATED SURPLUS - BEGINNING OF YEAR	740,090,750	740,090,750	721,630,376
ACCUMULATED SURPLUS - END OF YEAR	\$ 754,965,591	\$ 761,070,797	\$ 740,090,750

CITY OF NANAIMO
CONSOLIDATED STATEMENT OF CHANGES IN NET FINANCIAL ASSETS
for the year ended December 31, 2017 , with comparative figures for 2016

	2017 Budget (Note 14)	2017	2016
ANNUAL SURPLUS	\$ 14,874,841	\$ 20,980,047	\$ 18,460,374
Acquisition of tangible capital assets	(58,597,556)	(25,748,499)	(27,932,015)
In kind donations of capital assets	-	(227,079)	-
Developer contributed capital assets	-	(3,724,488)	(8,126,066)
	(58,597,556)	(29,700,066)	(36,058,081)
Amortization of tangible capital assets	23,527,325	23,319,708	22,926,296
Loss on disposal of tangible capital assets	-	(852,358)	1,533,210
Proceeds on sale of tangible capital assets	-	2,145,758	51,774
	(35,070,231)	(5,086,958)	(11,546,801)
Acquisition of inventories of supplies	-	(4,551,869)	(3,539,706)
Acquisition of prepaid expenses	-	(1,190,316)	(1,145,403)
Consumption of inventories of supplies	-	4,308,363	3,386,788
Use of prepaid expenses	-	1,161,956	1,940,719
	-	(271,866)	642,398
CHANGE IN NET FINANCIAL ASSETS	(20,195,390)	15,621,223	7,555,971
NET FINANCIAL ASSETS - BEGINNING OF YEAR	56,957,862	56,957,862	49,401,891
NET FINANCIAL ASSETS - END OF YEAR	\$ 36,762,472	\$ 72,579,085	\$ 56,957,862

CITY OF NANAIMO
CONSOLIDATED STATEMENT OF CASH FLOWS

for the year ended December 31, 2017, with comparative figures for 2016

	2017	2016
CASH PROVIDED BY (USED FOR)		
OPERATING TRANSACTIONS		
Annual Surplus	\$ 20,980,047	\$ 18,460,374
Non-cash items		
Amortization of tangible capital assets	23,319,708	22,926,296
Developer assets received	(3,724,488)	(8,126,066)
In kind donations of capital assets	(227,079)	-
(Gain) loss on disposal of tangible capital assets	(852,358)	1,533,210
Development cost charges recognized as revenue	(6,802,341)	(5,390,435)
Actuarial adjustment on long term debt	(867,932)	(748,340)
Change in non-cash operating assets and liabilities		
Accounts Receivable	(4,729,505)	2,809,965
Accounts payable	(941,851)	4,782,042
Deferred revenue	229,463	454,781
Inventories of supplies	(243,506)	(152,918)
Prepaid expenses	(28,360)	795,316
Net change in cash from operating transactions	26,111,798	37,344,225
CAPITAL TRANSACTIONS		
Cash used to acquire tangible capital assets	(25,748,499)	(27,932,015)
Proceeds from the sale of tangible capital assets	2,145,758	51,774
Net change in cash from capital transactions	(23,602,741)	(27,880,241)
INVESTING TRANSACTIONS		
Change in investments	(27,484,862)	(11,940,588)
FINANCING TRANSACTIONS		
Debt repayment	(2,221,857)	(3,099,953)
Deferred development cost charges	7,191,124	8,960,449
Proceeds from long term borrowing	1,500,000	-
Net change in cash from financing transactions	6,469,267	5,860,496
CHANGE IN CASH AND CASH EQUIVALENTS	(18,506,538)	3,383,892
CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR	69,589,008	66,205,116
CASH AND CASH EQUIVALENTS - END OF YEAR	\$ 51,082,470	\$ 69,589,008

CITY OF NANAIMO SCHEDULE OF OPERATIONS BY SEGMENT

for the year ended December 31, 2017

	City Admin	Corporate Services	Development Services	Fire	Police	Port of Nanaimo Centre	Parks and Recreation	Engineering and Public Works	Sewer System	Waterworks	Consolidated
Revenues											
Taxes	\$ 6,336,701	\$13,203,377	\$ 7,246,517	\$16,278,694	\$26,190,233	\$ 1,833,485	\$16,228,719	\$14,454,901	\$ -	\$ -	\$ 101,772,627
Payments in lieu of taxes	121,418	161,284	138,851	311,917	501,833	35,132	310,959	276,971	-	-	1,858,365
User fees	1,614,870	124,213	160,192	112,178	114,399	799,523	6,639,352	5,046,516	7,085,084	18,098,377	39,794,704
Developer assets	-	-	-	-	-	-	1,280,700	1,952,764	253,608	237,416	3,724,488
Other revenue	608,351	879,619	1,659,407	1,692,045	443,561	13,026	440,524	666,981	3,497	104,907	6,511,918
DCC revenue	-	-	-	-	-	-	1,249,298	2,061,472	1,158,852	2,332,719	6,802,341
Gov't operating transfers	105,224	172,133	357,212	270,311	1,628,162	1,149,168	600,053	257,627	90,000	-	4,629,890
Gov't capital transfers	-	3,637,130	-	-	-	-	-	107,874	-	-	3,745,004
Investment income	129,533	1,561,286	148,130	332,763	535,370	37,479	331,740	317,219	-	9,630	3,403,150
Building permits	-	-	1,885,202	-	-	-	-	-	-	-	1,885,202
Regional recreation sharing	-	-	-	-	-	-	1,113,566	-	-	-	1,113,566
Property rentals	30,000	-	328,481	17,850	281,213	-	251,444	31,558	-	21,000	961,546
Donations - capital	-	-	-	-	-	-	669,445	295,000	-	8,457	972,902
	8,946,097	19,739,042	11,923,992	19,015,758	29,694,771	3,867,813	29,115,800	25,468,883	8,591,041	20,812,506	177,175,703
Expenses											
Wages and salaries	4,837,998	6,315,874	5,851,974	14,630,512	4,976,016	1,652	13,591,921	9,308,918	1,036,921	3,240,844	63,792,630
Contracted services	2,477,697	3,325,669	2,325,460	1,285,686	22,936,251	1,725,315	8,135,172	7,980,076	688,066	1,104,419	51,983,811
Amortization	385,189	1,052,646	570,322	601,407	328,584	1,623,555	3,244,668	9,150,128	755,019	5,608,190	23,319,708
Other	532,499	2,709,831	2,121,032	78,764	170,413	24,120	1,025,958	(2,687,265)	1,983,516	3,044,024	9,002,892
Materials and supplies	451,545	214,583	203,562	726,724	101,760	76,139	1,944,578	2,969,849	228,973	843,825	7,761,538
Interest payments on debt	-	-	-	122,005	-	430,457	(98,763)	6,720	-	727,016	1,187,435
(Gain) loss on disposal of assets	(1,700)	(1,289,953)	(48,735)	13,108	67,438	-	(4,854)	317,617	62,995	31,726	(852,358)
	8,683,228	12,328,650	11,023,615	17,458,206	28,580,462	3,881,238	27,838,680	27,046,043	4,755,490	14,600,044	156,195,656
ANNUAL SURPLUS (DEFICIT)	262,869	7,410,392	900,377	1,557,552	1,114,309	(13,425)	1,277,120	(1,577,160)	3,835,551	6,212,462	20,980,047
Capital projects	\$ 14,475	\$ 406,818	\$ -	\$ 150,606	\$ 366,279	\$ 51,844	\$10,276,316	\$ 9,871,534	\$ 4,520,230	\$ 4,041,964	\$ 29,700,066

CITY OF NANAIMO

SCHEDULE OF OPERATIONS BY SEGMENT

for the year ended December 31, 2016

	City Admin	Corporate Services	Development Services	Fire	Police	Port of Nanaimo Centre	Parks and Recreation	Engineering and Public Works	Sewer System	Waterworks	Consolidated
Revenues											
Taxes	\$ 5,295,440	\$10,881,034	\$ 8,017,066	\$15,683,358	\$25,137,578	\$ 2,551,060	\$15,165,931	\$15,274,639	\$ -	\$ -	98,006,106
Payments in lieu of taxes	82,131	108,001	124,343	243,246	389,879	39,566	235,220	236,874	-	-	1,459,260
User fees	1,479,305	143,773	456,739	106,850	104,369	2,043,538	6,664,001	4,499,119	6,291,738	16,558,860	38,348,292
Developer assets	-	-	-	-	-	-	2,708,146	4,206,303	779,385	432,232	8,126,066
Other revenue	545,852	743,379	1,674,497	1,483,337	413,105	19,460	412,217	503,473	97	86,498	5,881,915
DCC revenue	-	-	-	-	-	-	4,878	178,666	4,327,736	879,155	5,390,435
Gov't operating transfers	55,907	105,107	406,074	180,576	1,959,568	1,036,015	401,782	186,578	-	-	4,331,607
Gov't capital transfers	-	3,587,994	-	-	-	-	64,025	27,399	-	-	3,679,418
Investment income	103,656	1,287,828	156,931	306,994	492,056	49,935	296,866	309,027	-	6,713	3,010,006
Building permits	-	-	1,619,320	-	-	-	-	-	-	-	1,619,320
Regional recreation sharing	-	-	-	-	-	-	1,091,640	-	-	-	1,091,640
Property rentals	30,000	-	344,231	21,450	295,627	-	280,726	28,882	-	21,000	1,021,916
Donations - capital	-	-	337,600	-	-	-	211,598	417,260	1,000	51,195	1,018,653
MFA refunds	-	-	-	-	-	-	-	4,449	-	-	4,449
	7,592,291	16,857,116	13,136,801	18,025,811	28,792,182	5,739,574	27,537,030	25,872,669	11,399,956	18,035,653	172,989,083
Expenses											
Wages and salaries	4,196,929	5,881,887	6,346,373	14,138,523	5,327,685	671	13,429,260	8,972,073	1,018,293	3,014,076	62,325,770
Contracted services	2,216,834	3,043,556	2,224,944	1,273,856	23,476,187	2,896,935	5,921,727	6,789,216	838,345	1,232,046	49,913,646
Amortization	454,236	701,368	816,487	605,087	323,435	1,623,554	3,118,984	9,122,369	657,189	5,503,587	22,926,296
Other	481,002	2,664,033	2,091,583	81,607	170,978	48,089	997,249	(2,631,838)	1,921,874	2,935,573	8,760,150
Materials and supplies	477,402	195,049	296,819	647,590	100,970	55,440	1,932,432	2,548,002	265,340	809,498	7,328,542
Interest payments on debt	40,055	-	-	133,653	-	882,358	(74,456)	-	-	759,485	1,741,095
Loss on disposal of assets	-	-	-	35,296	-	-	255,978	1,133,474	50,043	58,419	1,533,210
	7,866,458	12,485,893	11,776,206	16,915,612	29,399,255	5,507,047	25,581,174	25,933,296	4,751,084	14,312,684	154,528,709
ANNUAL SURPLUS (DEFICIT)	(274,167)	4,371,223	1,360,595	1,110,199	(607,073)	232,527	1,955,856	(60,627)	6,648,872	3,722,969	18,460,374
Capital projects	\$ 211,701	\$ 291,057	\$ 373,842	\$ 227,274	\$ 3,114	\$ 22,167	\$ 6,418,290	\$10,510,522	\$ 7,086,442	\$10,913,672	36,058,081

CITY OF NANAIMO
SCHEDULE OF TANGIBLE CAPITAL ASSETS
for the year ended December 31, 2017

	ASSETS				ACCUMULATED AMORTIZATION				NET BOOK VALUE	
	Balance December 31, 2016	Additions	Disposals	Transfers	Balance December 31, 2017	Balance December 31, 2016	Additions	Disposals		Balance December 31, 2017
Land	\$ 87,649,479	\$ 5,258,995	\$ 584,355	\$ -	\$ 92,324,119	\$ -	\$ -	\$ -	\$ -	\$ 92,324,119
Land improvements	35,166,074	1,518,227	171,091	208,726	36,721,936	14,368,433	1,290,592	171,091	15,487,934	21,234,002
Leasehold improvements	2,133,740	-	27,492	-	2,106,248	1,818,213	41,497	16,244	1,843,466	262,782
Marine structures	867,490	240,734	279,000	-	829,224	731,002	26,450	279,000	478,452	350,772
Buildings	193,020,392	621,254	216,500	3,113	193,428,259	70,762,670	5,228,190	149,062	75,841,798	117,586,461
Vehicles and equipment	31,647,962	2,664,168	1,615,714	158,177	32,854,593	19,005,607	1,972,711	1,267,249	19,711,069	13,143,524
IT Infrastructure	9,055,311	277,120	45,428	213,941	9,500,944	8,268,803	438,767	44,945	8,662,625	838,319
Drainage	104,061,927	1,221,556	400,450	397,982	105,281,015	29,351,384	1,615,924	393,267	30,574,041	74,706,974
Transportation	301,897,321	2,892,099	942,101	282,456	304,129,775	165,462,950	6,655,070	764,630	171,353,390	132,776,385
Sewer	41,847,292	2,097,348	201,300	1,547,731	45,291,071	12,025,825	749,686	138,305	12,637,206	32,653,865
Water	251,253,107	2,886,453	296,741	3,640,168	257,482,987	65,106,910	5,300,821	262,979	70,144,752	187,338,235
Work In Progress	9,430,420	10,022,112	-	(6,452,294)	13,000,238	-	-	-	-	13,000,238
	\$ 1,068,030,515	\$ 29,700,066	\$ 4,780,172	\$ -	\$ 1,092,950,409	\$ 386,901,797	\$ 23,319,708	\$ 3,486,772	\$ 406,734,733	\$ 686,215,676

CITY OF NANAIMO
SCHEDULE OF TANGIBLE CAPITAL ASSETS

for the year ended December 31, 2016

	ASSETS				ACCUMULATED AMORTIZATION				NET BOOK VALUE	
	Balance December 31, 2015	Additions	Disposals	Transfers	Balance December 31, 2016	Balance December 31, 2015	Additions	Disposals		Balance December 31, 2016
Land	\$ 85,701,341	\$ 3,071,774	\$ 1,123,636	\$ -	\$ 87,649,479	\$ -	\$ -	\$ -	\$ -	\$ 87,649,479
Land improvements	28,963,652	3,625,590	446,158	3,022,990	35,166,074	13,604,535	1,206,898	443,000	14,368,433	20,797,641
Leasehold improvements	2,174,294	30,738	111,891	40,599	2,133,740	1,865,382	64,722	111,891	1,818,213	315,527
Marine structures	867,490	-	-	-	867,490	702,915	28,087	-	731,002	136,488
Buildings	192,493,386	937,702	517,724	107,028	193,020,392	65,780,144	5,211,712	229,186	70,762,670	122,257,722
Vehicles and equipment	30,813,100	2,249,255	1,483,428	69,035	31,647,962	18,622,072	1,833,819	1,450,284	19,005,607	12,642,355
IT Infrastructure	9,092,424	27,188	106,182	41,881	9,055,311	7,867,886	507,099	106,182	8,268,803	786,508
Drainage	101,499,787	2,549,881	36,057	48,316	104,061,927	27,773,662	1,596,438	18,716	29,351,384	74,710,543
Transportation	297,826,583	4,133,400	555,562	492,900	301,897,321	159,371,904	6,643,004	551,958	165,462,950	136,434,371
Sewer	36,200,686	5,487,692	289,700	448,614	41,847,292	11,613,626	651,856	239,657	12,025,825	29,821,467
Water	242,097,287	9,072,681	385,364	468,503	251,253,107	60,244,093	5,182,661	319,844	65,106,910	186,146,197
Work In Progress	9,298,106	4,872,180	-	(4,739,866)	9,430,420	-	-	-	-	9,430,420
	\$1,037,028,136	\$ 36,058,081	\$ 5,055,702	\$ -	\$1,068,030,515	\$ 367,446,219	\$ 22,926,296	\$ 3,470,718	\$ 386,901,797	\$ 681,128,718

CITY OF NANAIMO

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended December 31, 2017

The City of Nanaimo (the City) was incorporated December 24, 1874 under a statute of the Province of British Columbia now known as the *Community Charter*. The principal activities of the City are preservation, protection and enhancement of the quality of life in Nanaimo through the facilitation of municipal services in an equitable, efficient and effective manner.

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

The City prepares its consolidated financial statements in accordance with Canadian public sector accounting standards as prescribed by the Public Sector Accounting Board (PSAB) of the Chartered Professional Accountants of Canada. The following include significant policies that have been adopted by the City:

(a) Basis of Presentation

The City's resources and operations are segregated into general, water and sewer, capital and reserve funds for accounting and financial reporting purposes. The financial statements reflect the assets, liabilities, revenues and expenses of these funds.

Consolidated Entities

The reporting entity is comprised of all organizations controlled by the City. These organizations include the Nanaimo Economic Development Corporation.

(b) Basis of Accounting

The City follows the accrual method of accounting for revenues and expenses. Revenues are normally recognized in the year in which they are earned and measurable. Expenses are recognized as they are incurred and measurable as a result of the delivery of goods or services and/or upon the creation of a legal obligation to pay. Expenses paid in the current period and attributable to a future period are recorded as prepaid.

(c) Cash and Cash Equivalents

Cash equivalents include short-term highly liquid investments with a term to maturity of 90 days or less at acquisition. Cash equivalents also include investments in the Municipal Finance Authority of British Columbia (MFA) Money Market Funds which are recorded at cost plus earnings reinvested in the funds.

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(d) Accounts Receivable

Accounts receivable are presented net of an allowance for doubtful accounts and therefore represent amounts expected to be collected.

(e) Development Cost Charges

Deferred development cost charges are restricted by legislation to expenditures on capital infrastructure and related debt servicing costs and operating projects. These amounts are deferred upon receipt and recognized as revenue when the expenditures are incurred in accordance with the restrictions.

(f) Temporary Investments

Temporary investments consist of term deposits and debentures which are expected to be held for a term exceeding 90 days. Investments are recorded at cost. When, in the opinion of management, there is a decline in value, other than a temporary decline, investments are written down to their net realizable value.

(g) Compensated Absences and Termination Benefits

The City and its employees make contributions to the Municipal Pension Plan. As this plan is a multi-employer plan, contributions are expensed as incurred. Compensated absences and termination benefits also accrue to the City's employees. The liabilities related to these termination benefits and earned sick leave are actuarially determined based on service and best estimates of retirement ages and expected future salary and wage increases. The liabilities under these benefit plans are accrued based on projected benefits prorated as employees render services necessary to earn the future benefits. Actuarial gains and losses on the accrued benefit obligation arise from differences between actual and expected experience and from changes in the actuarial assumptions used to determine the accrued benefit obligation. The net accumulated actuarial gains and losses are amortized over the average remaining service period of the active employees.

(h) Deferred Revenue

The City defers a portion of the revenue collected from permits, licenses and other fees and recognizes this revenue in the year in which related inspections are performed or other related expenditures are incurred.

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(i) Debt

Debt is presented net of repayments and actuarial adjustments.

(j) Non-Financial Assets

Non-financial assets are not available to discharge existing liabilities and are held for use in the provision of services. They may have useful lives extending beyond the current year and are not intended to be sold in the ordinary course of operations.

(i) Tangible Capital Assets

Tangible capital assets are comprised of capital assets and capital works in progress, and are recorded at cost, which includes amounts that are directly attributable to acquisition, construction, development or betterment of the assets. The cost of the tangible capital assets, excluding land, is amortized on a straight-line basis over the estimated useful lives of the assets, commencing at the time the assets are available for use.

Estimated useful lives in years are as follows:

Asset	
Land Improvements	2-80
Leasehold Improvements	15-30
Marine Structures	15-35
Buildings	10-40
Vehicles and Equipment	2-25
IT Infrastructure	2-10
Drainage	2-75
Transportation - Linear Infrastructure, Lighting and Signals	10-80
Sewer - Linear Infrastructure and Equipment	25-60
Water - Linear Infrastructure and Equipment	8-80

Tangible capital assets are written down to their residual value when conditions indicate that they no longer contribute to the City's ability to provide goods and services, or when the value of the future economic benefits associated with the asset is less than the book value of the asset.

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(j) Non-Financial Assets (continued)

(ii) Contribution of Tangible Capital Assets

Subdivision streets, lighting, sidewalks, drainage and other infrastructure assets are required to be provided by subdivision developers. Tangible capital assets received from developers are recorded at their fair values at the date of receipt and also recorded as revenue. The City is not involved in the construction and does not budget for assets received from developers.

(iii) Natural Resources, Works of Art and Cultural and Historical Assets

Natural Resources, works of art, and cultural and historical assets are not recognized as assets in the financial statements.

(iv) Interest Capitalization

The City does not capitalize interest costs associated with the acquisition or construction of a tangible capital asset.

(v) Leased Tangible Capital Assets

Leases which transfer substantially all of the benefits and risks incidental to ownership of property are accounted for as leased tangible capital assets with a corresponding lease liability. All other leases are accounted for as operating leases and the related payments are charged to expenses as incurred.

(vi) Inventories of Supplies

Inventories of supplies are recorded at cost, net of an allowance for obsolete stock. Cost is determined on a weighted average basis.

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(k) Contaminated Sites

A liability for contaminated sites is recognized when a site is not in productive use and the following criteria are met:

- i. An environmental standard exists;
- ii. Contamination exceeds the environmental standard;
- iii. The City is directly responsible or accepts responsibility;
- iv. It is expected that future economic benefits will be given up; and
- v. A reasonable estimate of the amount can be made.

The liability is recognized as management's estimate of the cost of post-remediation including operation, maintenance and monitoring that are an integral part of the remediation strategy for a contaminated site.

(l) Revenue Recognition

(i) Taxation Revenue

Annual levies for non-optional municipal services and general administrative services are recorded as taxes for municipal purposes. Levies imposed by other taxing authorities are not included as taxes for municipal purposes. Taxes are recognized as revenue in the year they are levied.

Through the BC Assessment appeal process, taxes may be adjusted by way of supplementary roll adjustments. The impacts of these adjustments on taxes are recognized at the time they are awarded.

(ii) Development Cost Charges

Development cost charges are recognized as revenue during the period in which the related costs are incurred.

(iii) Government Transfers

Government transfers without stipulations restricting their use are recognized in the financial statements as revenue in the period in which the transfers are authorized. Government transfers with stipulations restricting their use are recognized in the financial statements as revenues in the period in which eligible expenses are incurred provided they are authorized and meet eligible criteria.

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(m) Use of Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Significant areas requiring the use of management estimates relate to the determination of compensated absences and termination benefits, collectability of accounts receivable, useful lives of tangible assets for calculation of amortization and provisions for contingencies. Actual results could differ from those estimates. Adjustments, if any, will be reflected in operations in the period of settlement.

NOTE 2 - ACCOUNTS RECEIVABLE

	<u>2017</u>	<u>2016</u>
Utilities	\$ 11,246,646	\$ 6,788,646
Property Taxes	3,302,159	3,720,173
Trade and Other	1,734,615	1,492,159
Due from Provincial Government	1,261,738	1,166,388
Municipal Finance Authority Debt Reserve	902,317	885,056
Due from Federal Government	534,496	784,213
Interest on Investments	991,960	723,596
Due from Regional Government	216,681	152,009
	<u>\$ 20,190,612</u>	<u>\$ 15,712,240</u>

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 3 - DEVELOPMENT COST CHARGES RECEIVABLE

	<u>Water</u> <u>Distribution</u>	<u>Roads</u>	<u>Drainage</u>	<u>Sewer</u>	<u>Parks</u>	<u>Water</u> <u>Supply</u>	<u>2017</u>	<u>2016</u>
Installments:								
2016	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 156,258
2017	8,516	112,183	16,369	23,777	45,605	153,504	359,954	156,259
2018	4,801	63,832	9,222	13,394	25,947	86,500	203,696	-
	<u>\$ 13,317</u>	<u>\$ 176,015</u>	<u>\$ 25,591</u>	<u>\$ 37,171</u>	<u>\$ 71,552</u>	<u>\$ 240,004</u>	<u>\$ 563,650</u>	<u>\$ 312,517</u>

Development cost charges are collected on the approval of a subdivision or the issuance of a building permit. These funds assist the City in the cost of development, including constructing capital improvements, operating projects and the related debt servicing costs. Installments receivable represent funds due from developers within two years and are secured by irrevocable standby letters of credit and/or cash on deposit. No interest is charged on these outstanding installments.

NOTE 4 - TEMPORARY INVESTMENTS

	<u>2017</u>		<u>2016</u>	
	<u>Cost</u>	<u>Market</u>	<u>Cost</u>	<u>Market</u>
Temporary Investments	\$ 121,196,872	\$ 121,196,872	\$ 93,731,114	\$ 93,912,139
Debentures	18,954,800	18,669,441	18,935,696	18,889,165
	<u>\$ 140,151,672</u>	<u>\$ 139,866,313</u>	<u>\$ 112,666,810</u>	<u>\$ 112,801,304</u>

NOTE 5 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	<u>2017</u>	<u>2016</u>
Trade and Other	\$ 9,814,046	\$ 13,295,218
RCMP Contract	7,666,262	8,404,290
Deposits	6,703,412	5,072,714
Accrued wages and benefits	4,388,820	3,746,383
Contaminated sites	225,750	110,000
Other governments	1,082,910	569,642
	<u>\$ 29,881,200</u>	<u>\$ 31,198,247</u>

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 6 - COMPENSATED ABSENCES AND TERMINATION BENEFITS

The City provides certain post-employment benefits, non-vested sick leave, compensated absences and termination benefits to its employees. An actuarial valuation for these benefits was performed to determine the City's accrued benefit obligation as at December 31, 2016 and the results are extrapolated to December 31, 2017. The current valuation was completed in 2017. Significant assumptions used in the valuation include a discount rate of 4% (2016 - 4.75%), inflation of 1.75% (2016 - 2%) and compensation increases, excluding merit and promotion, of 2.75% (2016 - 3%). There is an unamortized actuarial loss of \$677,856 (2016 – gain of \$146,513).

	<u>2017</u>	<u>2016</u>
Actuarial Benefit Obligation, beginning of year	\$ 6,842,967	\$ 6,671,260
Unamortized Actuarial Gain, beginning of year	146,513	153,663
	<hr/>	<hr/>
	6,989,480	6,824,923
Current Service Cost	737,565	488,406
Interest Costs	309,023	313,517
Benefits Paid	(732,344)	(630,216)
Amortization of Actuarial (Gain) / Loss	60,952	(7,150)
	<hr/>	<hr/>
	7,364,676	6,989,480
	<hr/>	<hr/>
Actuarial Benefit Obligation, end of year	8,042,532	6,842,967
Unamortized Actuarial Gain / (Loss), end of year	(677,856)	146,513
	<hr/>	<hr/>
Accrued Benefit Liability, end of year	\$ 7,364,676	\$ 6,989,480

Actuarial gains and losses are amortized over 12 – 14 years, being the expected average remaining service period of the related employee groups, commencing the year after the gain or loss arises. The total expense recorded in the financial statements in respect of obligations under this plan amounts to \$1,107,540 (2016 - \$794,773).

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 7 - DEFERRED REVENUE AND OTHER LIABILITIES

	<u>2017</u>	<u>2016</u>
Tax Prepayments	\$ 11,825,590	\$ 11,577,802
Other Prepayments	5,384,657	5,402,982
	<u>\$ 17,210,247</u>	<u>\$ 16,980,784</u>

NOTE 8 - DEFERRED DEVELOPMENT COST CHARGES

	<u>2017</u>	<u>2016</u>
Deferred Development Cost Charges - beginning of year	\$ 42,228,902	\$ 38,658,888
Additions	6,396,603	8,224,116
Interest Earned	794,521	736,333
Revenue Recognized	(6,802,341)	(5,390,435)
	<u>\$ 42,617,685</u>	<u>\$ 42,228,902</u>

NOTE 9 - DEBT, NET OF MUNICIPAL FINANCE AUTHORITY (MFA) SINKING FUND DEPOSITS

The City issues debt instruments through the MFA pursuant to security issuing bylaws under authority of the *Community Charter* to finance certain capital expenditures.

\$42,335,511 (2016 – \$43,925,300) of debt is with the MFA. Payments of \$23,966,689 on the gross amount borrowed of \$66,350,000 are held in a sinking fund by the MFA. The rates of interest on the principal amount of the MFA debentures vary between 1.6% and 3.85% per annum.

	<u>2017</u>	<u>2016</u>
Total Outstanding Debt - beginning of year	\$ 43,925,300	\$ 47,773,593
Reduction of Long-term Debt	(3,089,789)	(3,848,293)
Proceeds from long-term borrowing	1,500,000	-
	<u>\$ 42,335,511</u>	<u>\$ 43,925,300</u>

The City of Nanaimo is subject to 'Liability Servicing Limits' as outlined in Section 174 of the *Community Charter*. The maximum value of liability servicing cost for a given year is 25% of a municipality's controllable and sustainable revenues for the previous year. The calculated liability servicing limit for the City of Nanaimo for 2017 at December 31, 2016 was \$38,379,597. The actual liability servicing cost was \$6,075,618, leaving \$32,303,979 of liability servicing capacity available.

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 9 - DEBT, NET OF MUNICIPAL FINANCE AUTHORITY (MFA) SINKING FUND DEPOSITS (CONTINUED)

Future payments on net outstanding debt over the next five years and thereafter are as follows:

<u>Year</u>	<u>General</u>	<u>Water</u>	<u>Total</u>
2018	\$ 2,586,747	\$ 870,032	\$ 3,456,779
2019	2,686,848	904,833	3,591,681
2020	2,790,928	941,026	3,731,954
2021	2,227,194	978,667	3,205,861
2022	2,256,386	1,017,814	3,274,200
Thereafter	10,148,462	14,926,574	25,075,036
	<u>\$ 22,696,565</u>	<u>\$ 19,638,946</u>	<u>\$ 42,335,511</u>

<u>Bylaw #</u>	<u>MFA Issue #</u>		<u>Interest Rate %</u>	<u>Year Matures</u>	<u>Balance Outstanding</u>	
					<u>2017</u>	<u>2016</u>
<u>General Fund - Tax Supported</u>						
5425	72	Leisure and Aquatic Centre	2.10	2020	\$ 966,732	\$ 1,261,630
5457	73	Leisure and Aquatic Centre	1.60	2020	880,801	1,149,486
5750	99	Port of Nanaimo Centre	1.75	2026	8,206,571	8,952,209
5750	101	Port of Nanaimo Centre	2.25	2027	8,952,209	9,669,168
7050	102	Fire Station #4	2.25	2027	2,238,052	2,417,292
N/A	N/A	Garbage Trucks Equipment	1.81	2022	1,452,200	-
					<u>22,696,565</u>	<u>23,449,785</u>
<u>Waterworks Fund - User Fee Supported</u>						
7127	126	Water Treatment Plant	3.85	2033	11,403,371	11,905,777
7127	127	Water Treatment Plant	3.30	2034	8,235,575	8,569,738
					<u>19,638,946</u>	<u>20,475,515</u>
					<u>\$ 42,335,511</u>	<u>\$ 43,925,300</u>

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 10 - TANGIBLE CAPITAL ASSETS

<u>Net Book Value</u>	<u>2017</u>	<u>2016</u>
Land	\$ 92,324,119	\$ 87,649,479
Land Improvements	21,234,002	20,797,641
Leasehold Improvements	262,782	315,527
Marine Structures	350,772	136,488
Buildings	117,586,461	122,257,722
Vehicles and Equipment	13,143,524	12,642,355
IT Infrastructure	838,319	786,508
Drainage	74,706,974	74,710,543
Transportation	132,776,385	136,434,371
Sewer	32,653,865	29,821,467
Water	187,338,235	186,146,197
	<hr/>	<hr/>
	673,215,438	671,698,298
Work In Progress	13,000,238	9,430,420
	<hr/>	<hr/>
	<u>\$ 686,215,676</u>	<u>\$ 681,128,718</u>

See schedule of tangible capital assets (page 9) for more information. There were no write downs of tangible capital assets for 2016 and 2017. Developer contributed assets recognized in 2017 were \$3,724,488 (2016 - \$8,126,066) recorded at fair value at the time of receipt. These include transportation, drainage, sewer and water infrastructure and the land under these assets.

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 11 - ACCUMULATED SURPLUS

	<u>2017</u>	<u>2016</u>
Reserve Accounts (Note 22)	\$ 65,325,545	\$ 59,153,370
Surplus - General	5,499,908	5,139,416
Surplus - Sewer System	6,834,001	6,765,372
Surplus - Waterworks	5,545,156	5,430,316
Investment in Tangible Capital Assets (Note18)	643,880,165	637,203,418
Community Works Reserve Fund (Gas Tax Agreement)	5,450,615	6,136,926
Equipment Depreciation Reserve	7,516,016	6,148,706
Facility Development (Recreation) Reserve	3,125,384	2,133,321
Property Sales Reserve	2,325,949	1,183,092
Knowles Estate Reserve	420,076	435,516
Parkland Dedication Reserve	638,458	375,527
Old City Neighborhood Parking Reserve	88,896	87,227
General Asset Management Reserve	10,148,379	7,551,309
Sewer Asset Management Reserve	1,146,300	834,516
Water Asset Management Reserve	2,664,841	1,135,280
Regional Emissions Reduction Reserve	461,108	377,438
	<u>\$ 761,070,797</u>	<u>\$ 740,090,750</u>

NOTE 12 - COMMITMENTS AND CONTINGENCIES

(a) Liability Claims

In the ordinary course of business, various claims and lawsuits are brought against the City. The City records an accrual in respect of legal claims that are likely to be successful and for which a liability amount is reasonably determinable. The remaining claims, should they be successful as a result of litigation, will be recorded when a liability is likely and determinable. Liability insurance is carried by the City, subject to a deductible of \$25,000 per claim.

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 12 - COMMITMENTS AND CONTINGENCIES (CONTINUED)

(b) BC Assessment Authority Appeals

As at December 31, 2017, there were various appeals pending with respect to assessed values of properties. The outcome of those appeals may result in adjustments to property taxes receivable for the current and prior years. The City makes a provision against property taxes receivable for the impact of appeals where the losses are likely and the amounts are reasonably determinable.

(c) Joint and Several Liabilities

The City has a contingent liability with respect to debentures of the Regional District of Nanaimo and the Regional Hospital District of Nanaimo, to the extent provided for in their respective Acts of Incorporation. Management does not consider payment under this contingency to be likely and therefore no amounts have been accrued.

The City issues its debt instruments primarily through the MFA. Demand notes are executed in connection with each debenture whereby the City may be required to pay certain amounts to the Regional District of Nanaimo. These demand notes of \$1,871,727 (2016 – \$1,871,727) are contingent in nature and given the low likelihood of payment are not reflected in the accounts.

The City is a participant in the Municipal Insurance Association of British Columbia (the Association). Should the Association pay out claims in excess of premiums received, it is possible that the City, along with other participants, would be required to contribute towards the deficit.

(d) Subsidence of Mines

Continued existence of abandoned underground mines has resulted in risk to private land and public roads due to potential collapse or instability. The full impact of the abandoned mines and any potential liabilities are unknown at this time. No determination of the City's liability, if any, has been made and no estimate of potential loss can be made or recorded at this time. A liability will be recorded if remediation costs are determined to be likely and the amounts are reasonably determinable.

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 12 - COMMITMENTS AND CONTINGENCIES (CONTINUED)

(e) Commitments

The City has \$14,500,000 (2016 - \$7,800,000) in open purchase orders at year end which have not been recorded in the financial statements. The funding for the majority of these obligations has been set aside in reserves for future expenditures. These amounts will be recorded in the period that the goods and services, to which they relate, are received.

(f) Guarantees

The City has guaranteed the amount of a \$2,000,000 line of credit for the Port Theatre Society. Management considers the likelihood of payment on the guarantee to be low.

NOTE 13 - CEMETERY CARE FUND

The City operates the cemetery and maintains a cemetery perpetual care fund in accordance with the *Cremation, Interment and Funeral Services Act*. The trust fund assets and liabilities are not included in the consolidated financial statements. At December 31, 2017, the balance of funds held in trust was \$567,918 (2016 - \$556,668).

NOTE 14 - ANNUAL BUDGET

These financial statements include the Annual Budget as approved by Council on May 2, 2017. No amendments subsequent to this date have been included. The following is a reconciliation of the budget presentation required for the financial statements and the annual financial plan bylaw:

	<u>2017</u>
Annual Budgeted Surplus - Statement of Operations	\$ 14,867,341
Cemetery Care Fund - not in reporting entity	7,500
	<hr/>
Annual Surplus from the 2017 Financial Plan	14,874,841
Amortization, not funded	23,527,325
Capital Expenditures	(58,597,556)
Principal Repayment of Debt	(3,041,989)
Transfers from Accumulated Surplus	23,237,379
	<hr/>
Net Annual Budget - as approved	\$ -

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 15 - TAXATION AND PAYMENTS IN LIEU

	<u>Municipal</u>	<u>Other</u>	<u>2017</u> <u>Total</u>	<u>2016</u> <u>Total</u>
Property Taxes	\$ 95,952,570	\$ 60,836,867	\$ 156,789,437	\$ 151,991,685
Local Improvements Frontage Fees	-	-	-	2,119
Business Improvement Area Levies	40,774	-	40,774	231,923
Vancouver Island Regional Library	4,332,949	-	4,332,949	4,108,327
Taxes in Lieu of Licenses	1,446,334	-	1,446,334	1,423,278
Payments in Lieu of Taxes	1,858,365	537,974	2,396,339	1,946,586
	<u>\$ 103,630,992</u>	<u>\$ 61,374,841</u>	<u>\$ 165,005,833</u>	<u>\$ 159,703,918</u>
			<u>2017</u>	<u>2016</u>
Less Collections for Other Governments:				
Province of British Columbia (School Tax)			\$ 38,054,892	\$ 38,128,393
Regional District of Nanaimo			18,450,297	17,334,012
Nanaimo Regional Hospital District			3,892,423	3,742,866
Other Agencies			977,229	1,033,281
			<u>61,374,841</u>	<u>60,238,552</u>
Taxation and Payments in Lieu			<u>\$ 103,630,992</u>	<u>\$ 99,465,366</u>

NOTE 16 - USER FEES AND SALES OF SERVICES

	<u>2017</u>	<u>2016</u>
Waterworks	\$ 18,098,377	\$ 16,558,860
Recreation Programs	6,639,352	6,664,001
Sewer System	7,085,084	6,291,738
Garbage Collection	4,395,988	3,776,182
Vancouver Island Conference Centre	799,523	2,043,538
Public Works	650,528	722,937
Parking	1,590,319	1,454,039
Other	308,956	625,778
Community Safety	226,577	211,219
	<u>\$ 39,794,704</u>	<u>\$ 38,348,292</u>

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 17 - TRANSFERS FROM OTHER GOVERNMENTS

	<u>2017</u>	<u>2016</u>
<u>Federal</u>		
Gas Tax	\$ 3,637,130	\$ 3,587,994
Other	77,527	76,185
	<u>3,714,657</u>	<u>3,664,179</u>
<u>Provincial</u>		
Casino Gaming	2,863,235	2,593,933
Revenue Sharing	1,180,215	1,211,761
Other	366,479	329,784
	<u>4,409,929</u>	<u>4,135,478</u>
<u>Regional District of Nanaimo</u>		
Other	250,308	211,368
Total Transfers from Other Governments	<u>\$ 8,374,894</u>	<u>\$ 8,011,025</u>
Transfers from Other Governments - Capital	\$ 3,745,004	\$ 3,679,418
Transfers from Other Governments - Operating	4,629,890	4,331,607
Total Transfers from Other Governments	<u>\$ 8,374,894</u>	<u>\$ 8,011,025</u>

NOTE 18 - INVESTMENT IN TANGIBLE CAPITAL ASSETS

	<u>2017</u>	<u>2016</u>
Investment in Tangible Capital Assets - beginning of year	\$ 637,203,418	\$ 621,808,324
Add:		
Capital Additions	29,700,066	36,058,081
Reductions in Long-term Debt	3,089,789	3,848,293
Less:		
Proceeds from long-term borrowing	(1,500,000)	-
Amortization	(23,319,708)	(22,926,296)
Net Book Value of Asset Disposals	(1,293,400)	(1,584,984)
Investment in Tangible Capital Assets - end of year	<u>\$ 643,880,165</u>	<u>\$ 637,203,418</u>

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 19 - MUNICIPAL PENSION PLAN

The City and its employees contribute to the Municipal Pension Plan (the Plan), a jointly trustee pension plan. The Board of Trustees, representing plan members and employers, is responsible for administering the plan, including investment of the assets and administration of benefits. The Plan is a multi-employer defined benefit pension plan. Basic pension benefits provided are based on a formula. The Plan has about 193,000 active members and approximately 90,000 retired members. Active members include approximately 38,000 contributors from Local Government.

Every three years, an actuarial valuation is performed to assess the financial position of the plan and adequacy of plan funding. The actuary determines an appropriate combined employer and member contribution rate to fund the plan. The actuary's calculated contribution rate is based on the entry-age normal cost method, which produces the long-term rate of member and employer contributions sufficient to provide benefits for average future entrants to the plan. This rate is then adjusted to the extent there is amortization of any funding surplus and will be adjusted for the amortization of any unfunded liability.

The most recent valuation for the Municipal Pension Plan as at December 31, 2015 indicated a \$2,224 million funding surplus for basic pension benefits on a going concern basis. As a result of the 2015 basic account actuarial valuation surplus and pursuant to the joint trustee agreement, \$1,927 million was transferred to the rate stabilization account and \$297 million of the surplus ensured the required contribution rates remained unchanged. During 2017, City of Nanaimo contributions to the plan were:

	<u>2017</u>	<u>2016</u>
Employer Portion	\$ 5,073,448	\$ 4,902,227
Employee Portion	4,196,419	4,128,271
	<u>\$ 9,269,867</u>	<u>\$ 9,030,498</u>

The next valuation will be as at December 31, 2018 with results available in 2019.

Employers participating in the plan record their pension expense as the amount of employer contributions made during the fiscal year (defined contribution pension plan accounting). This is because the plan records accrued liabilities and accrued assets for the plan in aggregate, resulting in no consistent and reliable basis for allocating the obligation, assets and cost to individual employers participating in the plan.

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 20 - FINANCIAL INSTRUMENTS

(a) Financial Risk and Fair Market Values

The City's financial instruments consist of cash and cash equivalents, accounts receivable, development cost charges receivable, temporary investments, accounts payable and accrued liabilities and debt. The City does not hold any asset-backed commercial paper or hedge funds. The financial risk is the risk to the City's earnings that arises from fluctuations in interest rates, foreign exchange rates, and the degree of volatility of these rates. The City does not use derivative instruments to reduce its exposure to interest rate risk nor foreign exchange risk as management does not consider the risks material. Based on available market information, the carrying value of the City's financial instruments approximates their fair value with the exception of temporary investments for which market values are disclosed in Note 4.

(b) Credit Risk

The City is not exposed to significant risk from its accounts receivables. The City's tax base has a significant number of participants which reduces the concentration of credit risk. Credit risk is further minimized as the City has the ability to expropriate land in the event of non-payment of property tax receivables.

NOTE 21 - COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform with the financial statement presentation adopted for the current year.

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 22 - RESERVES

	<u>Work in</u> <u>Progress</u>	<u>Available for</u> <u>Future</u> <u>Commitments</u>	<u>2017</u>	<u>2016</u>
<u>General Revenue Fund Reserve Accounts</u>				
Fire & Emergency Services	\$ 2,000	\$ 2,445,488	\$ 2,447,488	\$ 2,047,367
Parks & Recreation	-	104,281	104,281	207,950
Strategic Partnerships	30,728	-	30,728	250,000
General Capital	706,769	4,082,634	4,789,403	5,127,355
Prior Year Carry Forwards	3,880,471	-	3,880,471	4,367,140
Housing Legacy Reserve	93,564	2,234,756	2,328,320	2,415,652
Uncollected Taxes	-	2,570,566	2,570,566	2,112,533
Uninsured Claims	-	2,535,386	2,535,386	2,682,939
Allowance for Bad Debts	10,000	40,000	50,000	50,000
RCMP Contract	212,071	2,901,771	3,113,842	3,078,832
Information Technology Infrastructure	1,371,482	117,116	1,488,598	1,615,670
Sustainability Initiatives	391,422	175,654	567,076	726,731
Parking Reserve	292,346	825,237	1,117,583	619,765
Conference Centre	240,170	514,746	754,916	760,126
Snow Removal	-	-	-	400,000
Property Acquisition	-	1,563,383	1,563,383	1,963,077
Strategic Infrastructure	680,000	-	680,000	-
General Financial Sustainability	450,000	500,000	950,000	-
Colliery Dam Reserve	80,000	119,123	199,123	242,454
Photocopier Reserve	-	368,580	368,580	309,408
Casino Funds	-	1,186,846	1,186,846	723,611
	<u>8,441,023</u>	<u>22,285,567</u>	<u>30,726,590</u>	<u>29,700,610</u>
<u>Sewer Revenue Reserve Accounts</u>				
General Capital	3,248,952	7,363,931	10,612,883	10,833,018
Growth Related Projects	-	916	916	916
	<u>3,248,952</u>	<u>7,364,847</u>	<u>10,613,799</u>	<u>10,833,934</u>
<u>Waterworks Revenue Fund Reserve Accounts</u>				
General Capital	18,942,102	3,043,393	21,985,495	16,619,165
Growth Related Projects	-	1,900,000	1,900,000	1,900,000
Local Improvement Projects	-	99,661	99,661	99,661
	<u>18,942,102</u>	<u>5,043,054</u>	<u>23,985,156</u>	<u>18,618,826</u>
Total Reserve Accounts	<u>\$30,632,077</u>	<u>\$ 34,693,468</u>	<u>\$65,325,545</u>	<u>\$59,153,370</u>

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 23 - SEGMENT REPORTING

The City's operations and activities are organized and reported by Fund. City services are provided by departments and their activities are reported in these funds. See Schedule of Operations by Segment (page 7).

GENERAL REVENUE FUND

Certain departments have been separately disclosed in the segmented information, along with the services they provide as follows:

City Administration

The Chief Administrative Officer's office assists Council to establish its strategic direction for the City and takes the lead role in managing the implementation of policy direction established by Council. The Office also provides managerial leadership and direction to all City departments and operations.

The City Administration department is responsible for the City's regulatory services, including legislative services, and the bylaw, animal control, and parking functions.

Corporate Services

Providing service to both the internal organization and the community, the Corporate Services Department is responsible for Human Resources and Organizational Planning, Information Technology, Financial Services and Purchasing.

Development Services

Development Services is responsible for a variety of tasks relating to planning and development. This includes processing development applications and developing related policies and regulations. The Development Services Department is also the liaison to the Nanaimo Economic Development Corporation.

Fire

The Fire Department has the responsibility of protecting the City's citizens and infrastructure through prevention and quick and high quality response to fire, medical and other emergency incidents in the most effective and responsive manner possible. Fire services also include emergency management, planning and coordination functions.

CITY OF NANAIMO
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended December 31, 2017

NOTE 23 - SEGMENT REPORTING (CONTINUED)

Police

The City contracts the Royal Canadian Mounted Police to provide top quality policing services in Nanaimo. With administrative support services provided by City employees, the detachment provides all standard policing services, including response to emergency and non-emergency calls, criminal investigations and traffic safety measures.

Port of Nanaimo Centre

The operation of the Vancouver Island Conference Centre provides a full-service convention centre that hosts meetings, conferences, tradeshows, and weddings for up to 1,300 delegates.

Parks and Recreation

The Parks and Recreation department manages, facilitates and maintains a system of services, facilities, parks and open spaces and works to enhance the quality of life for the citizens of Nanaimo.

Engineering and Public Works

Engineering and Public Works is responsible for the planning, design, construction, operation and maintenance of the City's infrastructure including the City's water, sanitary sewer, drainage and transportation infrastructure. Department operations also include maintenance of the City's fleet, cemeteries, solid waste collection and recycling.

SEWER SYSTEM

The City Sanitary Sewer Utility is a self-funded entity that operates and maintains a sewer collection system that serves the City.

WATERWORKS

The City Waterworks Utility is a self-funded entity that delivers water to residential, commercial and industrial premises in Nanaimo. The Utility operates and maintains a supply system consisting of dams, transmission mains, reservoirs and treatment facilities as well as a distribution system.



City of Nanaimo

**Audit Findings Report
For the year ended December 31, 2017**

KPMG LLP

Prepared for the meeting on May 9, 2018

kpmg.ca/audit



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Executive summary

Purpose of this report

The purpose of this Audit Findings Report is to assist you, as members of the Finance and Audit Committee, in your review of the results of our audit of the consolidated financial statements of the City of Nanaimo as at and for the year ended December 31, 2017.

This Audit Findings Report builds on the Audit Plan we presented to the Finance and Audit Committee on December 13, 2017.

Changes from the Audit Plan

Due to the increased risks surrounding management override of controls, this resulted in KPMG performing additional procedures required for high risk audit engagements, which includes:

- Increased sample sizes for substantive procedures
- Increased levels of management inquiries
- Testing of management expense reports, and
- Detailed reviews of various workplace policies.

Audit risks and results

We discussed with you at the start of the audit a number of financial areas where we would focus the audit:

- Significant risk of management override of controls
- Tangible capital assets and deferred development cost charges
- Salaries and benefits
- Cash and investments
- Revenue and receivables management
- Expenses, procurement and payables

By focusing on these areas, we established an overall audit strategy and effectively targeted our audit procedures. We are satisfied that our audit work has appropriately dealt with these areas.

See pages 5 to 7.

Adjustments and differences

There were no uncorrected audit differences identified.

We identified a \$1.1 million reclassification adjustment from cash and cash equivalents to temporary investments that was accepted and corrected by Management.

We identified a \$1.3 million reclassification adjustment from other revenue to gain on disposal of assets that was accepted and corrected by Management.

We identified disclosure misstatements that were accepted and corrected by Management.

See page 10 and Appendix 3 (containing the Management Representation Letter).

*This Audit Findings Report should not be used for any other purpose or by anyone other than the Finance and Audit Committee. 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

Finalizing the audit

We have completed the audit of the consolidated financial statements, with the exception of certain remaining procedures, which include amongst others:

- completing our discussions with the Finance and Audit Committee.
- obtaining evidence of Council's approval of the financial statements.
- obtaining the signed management representation letter.
- completing subsequent event review procedures up to the date of Council approval of the financial statements, including updating our discussions with management regarding any changes to our understanding of legal matters.

We will update you 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.

Critical accounting estimates

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

The critical areas of estimates relate to:

- Compensated absences and termination benefits
- Collectability of accounts receivables
- Useful lives of tangible assets
- Provisions for contingencies

See page 8.

Control and other observations

The significant deficiencies in internal control over financial reporting that have come to our attention relate to the following:

- Whistleblower policies
- Expense report review, authorization and policies
- Consistency of hiring practices
- Governance understanding and responsibilities

We have identified other observations with respect to Reserve transfers.

See page 11 and Appendix 4 (containing the Management Letter).

Independence

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

Significant accounting policies and practices

There have been no initial selections of, or changes to, significant accounting policies and practices to bring to your attention.

Financial statement presentation and disclosure

The presentation and disclosure of the financial statements are, in all material respects, in accordance with Public Sector Accounting Standards.

Audit risks and results (significant risks)

Inherent risk of material misstatement is the susceptibility of a balance or assertion to misstatement which could be material, individually or when aggregated with other misstatements, assuming that there are no related controls. We highlight our significant findings in respect of significant financial reporting risks, as well as any additional significant risks identified.

Significant financial reporting risks	Why	Our response and significant findings
Risk of management override	<p>This is a presumed fraud risk.</p> <p>Although the level of risk of management override of controls will vary from entity to entity, professional standards presume the risk of management override of controls is nevertheless present in all entities and requires the performance of specific procedures to address this presumed risk.</p>	<p>As the risk is not rebuttable, our audit methodology incorporates the required procedures in professional standards to address this risk. As such, we performed the required procedures under professional standards:</p> <ul style="list-style-type: none"> ● We used KPMG's Data and Analytics tools to select unusual or unexpected journal entries impacting revenue, including unusual journal entry pairings. ● We tested material journal entries made in the preparation of the year-end financial statements, entries potentially related to fraud or management override of controls, and inspected the relevant documentation for authorization and appropriateness. ● We performed a retrospective review of estimates, including the assumptions used by management. ● We evaluated the business rationale of significant unusual transactions. <p>KPMG notes that a poor tone at the top has provided opportunities for management override, including an override of hiring processes and various workplace policies, such as the travel and expense policy, reporting serious matters policy and respectful workplace policy.</p> <p>Please refer to the management letter included in Appendix 4 for KPMG's observations and recommendations. We are satisfied that our audit work has appropriately addressed the risk of management override.</p>

Audit risks and results (significant accounts)

We identified other areas of focus for our audit in our discussion with you in the Audit Plan.

Significant findings from the audit regarding other areas of focus are as follows:

Other areas of focus	Why	Our response and significant findings
Tangible capital assets and developer contributed capital assets	As this is the largest asset balance for the City, we have focused on testing the existence and accuracy of current year capital acquisitions, disposals and work in progress transfers, including developer contributed capital assets.	<ul style="list-style-type: none"> • We substantively tested asset additions by agreeing amounts to invoices or other supporting documentation. • We performed a substantive analytical procedure comparing expected amortization expense to actual. • We performed testing over the developer contributed tangible capital assets by obtaining reports of assets contributed during the year and agreeing these reports to supporting approval of subdivisions. • We performed inquiries with the engineering department members on completeness of the listings provided and the process used to develop the valuation estimates. • Donated assets were verified to engineer cost estimates and internally developed estimates as applicable.
Salaries and benefits	As this is the largest expense for the City, we have focused on testing the completeness and accuracy of the salaries and benefits balances.	<ul style="list-style-type: none"> • We performed a predictive substantive analytical procedure for both payroll expense and payroll accruals. In each case, our predictive analysis or expectation was within an acceptable range from the actual payroll expense, or payroll accrual recorded in the financial statements. • We tested the completeness and accuracy of the underlying payroll data used in the development of our substantive analytical procedure including agreeing amounts to employment contracts. • We performed a review of assumptions and methods used in estimating the liability of future employee benefits to determine if the assumptions and methods used are reasonable and consistent with Public Sector Accounting Standards. • No issues or adjustments were noted.

Audit risks and results (significant accounts)

Other areas of focus	Why	Our response and significant findings
Cash and investments	We have focused on the completeness and existence of cash and cash equivalent balances given the significant number of bank accounts, variety of currencies and existence of margin accounts.	<ul style="list-style-type: none"> We confirmed cash and investment balances held as at December 31, 2017 with the appropriate financial institutions and reviewed bank reconciliations for all key operating accounts to identify and verify any significant period end reconciling items. No issues were identified in this testing.
Expenses, procurement and payables	Significant account due to account balance	<ul style="list-style-type: none"> We performed a search for unrecorded liabilities by testing payments made subsequent to year end and assessing completeness of liabilities and expenses. We performed analytical procedures comparing actual balances to expectations. We tested expense reports (at both the management and Council level) to assess appropriate review and compliance with the City's reimbursement policies. Please refer to the management letter included in Appendix 4 for KPMG's findings and recommendations.
Revenues and receivables management	Significant account due to account balance	<ul style="list-style-type: none"> We performed substantive analytical procedures over tax revenues based on BC Assessment Authority assessed values and Council approved property tax rates by class. We performed substantive analytical testing of revenue balances on a financial statement account level compared to prior year and budget. We assessed the City's revenue recognition in accordance with Public Sector Accounting Standards. No issues or adjustments were noted

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	Balance	KPMG comment
Compensated absences and termination benefits	\$7.4 million	<p>We performed substantive analytical procedures over the provision for payroll and vacation accruals prepared by Management.</p> <p>We assessed the reasonableness of the discount rates and assumptions used by Nexus, the City’s actuary.</p> <p>The current valuation was performed as at December 31, 2016 with results being extrapolated to December 31, 2017.</p>
Collectability of accounts receivable	\$20.2 million	<p>We performed substantive analytical procedures over the year-end accounts receivable balance.</p> <p>We concur with Management’s assessment that there is a low valuation risk associated with the City’s year-end accounts receivable balance.</p>
Useful lives of tangible assets	\$682.2 million (Useful lives of City assets range from 2 to 80 years)	<p>We verified the mathematical accuracy and agreed the tangible capital asset continuity schedules to supporting detail and performed substantive analytical procedures on amortization expense.</p> <p>We assessed the reasonability and consistency of Management’s estimate of useful lives for the various categories of assets. We noted no significant changes in estimates from the prior period, nor were there indications of management bias.</p>
Contaminated sites	\$0.2 million	<p>We obtained an understanding and assessed the reasonability of Management’s analysis of non-productive sites and associated liabilities</p> <p>We performed testing over the completeness and reasonability of identified sites.</p>
Provisions for contingencies	\$0.5 million	<p>We performed inquiries with management and reviewed meeting minutes and other documentation.</p> <p>We confirmed with external legal counsel the existence and status of known and potential claims that could result in loss to the City.</p> <p>We concur with management’s disclosure of litigation in the financial statements.</p>

We believe management’s process for identifying critical accounting estimates is considered adequate.

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 included in the Appendices.

We also highlight the following:

Form, arrangement, and content of the financial statements	Enhancements recommended to management; refer to the adjustments and differences discussion on the next page.
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Application of accounting pronouncements issued but not yet effective	See Appendix 7 for discussion of current developments in public sector accounting standards.
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Adjustments and differences

Adjustments and differences identified during the audit have been categorized as “Corrected adjustments” or “Uncorrected differences”. These include disclosure adjustments and differences. Professional standards require that we request of management 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.

We identified a reclassification adjustment of \$1.1 million from cash and cash equivalents to temporary investments. The adjusting entry was recorded by Management and did not result in a change to Annual Surplus or Accumulated Surplus.

We identified a reclassification adjustment of \$1.3 million from other revenue to gain on disposal of tangible capital assets. The adjusting entry was recorded by Management and did not result in a change to Annual Surplus or Accumulated Surplus.

We identified presentation and disclosure misstatements with respect to:

- The presentation of budgeted corporate service expenses in the Statement of Operations and annual budget note disclosure
- The presentation of gain/loss on disposal of tangible capital assets and proceeds from the sale of tangible capital assets in the Statement of Cash Flows
- The presentation of payments in lieu of taxes in the Schedule of Operations by Segment

Uncorrected differences

We did not identify differences that remain uncorrected.

Control observations

Significant deficiencies

In accordance with professional standards, we are required to communicate to the Finance and Audit Committee any control deficiencies that we identified during the audit and have determined to be significant deficiencies in internal control over financial reporting. We have communicated significant deficiencies identified during the audit in our management letter. Please refer to Appendix 4.

Other control observations

Other control deficiencies identified were also communicated in our management letter. Please refer to Appendix 4.

Appendices

Appendix 1: Required Communications

Appendix 2: Draft Auditors' Report

Appendix 3: Draft Management Representation letter

Appendix 4: Management Letter

Appendix 5: Background and Professional Standards

Appendix 6: Current Developments

Appendix 7: KPMG's Cyber Security Protocol

Appendix 8: Audit Trends

Appendix 1: 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** – the conclusion of our audit is set out in our draft auditors' report in Appendix 2.
- **Audit findings report** – as attached.
- **Management representation letter** – In accordance with professional standards, copies of the management representation letter are provided to the Finance and Audit Committee. See Appendix 3.
- **Engagement letter** – the objectives of the audit, our responsibilities in carrying out our audit, as well as Management's responsibilities, are set out in the engagement letter which has been previously provided. Document available upon request.
- **Independence** – we confirm that 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 applicable legislation or regulation from January 1, 2017 up until the date of this report.
- **Management letter** - we have issued a letter to management related to significant deficiencies in internal controls. See Appendix 4.

Appendix 2: Draft Auditors' Report

To the Mayor and Council

We have audited the accompanying consolidated financial statements of the City of Nanaimo, which comprise the consolidated statement of financial position as at December 31, 2017 and the consolidated statements of operations, changes in net financial assets and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information, including the schedules of operations by segment and tangible capital assets.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with Canadian public sector accounting standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform an audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the City of Nanaimo as at December 31, 2017, and its consolidated results of operations, its changes in net consolidated financial assets, and its consolidated cash flows for the year then ended in accordance with Canadian public sector accounting standards.

Appendix 3: Draft Management Representation Letter

KPMG LLP
PO Box 10426
777 Dunsmuir Street
Vancouver BC V7Y 1K3
Canada

Date of financial statement approval by council

Ladies and Gentlemen:

We are writing at your request to confirm our understanding that your audit was for the purpose of expressing an opinion on the consolidated financial statements (hereinafter referred to as "financial statements") of the City of Nanaimo ("the City") as at and for the period ended December 31, 2017.

We confirm that the representations we make in this letter are in accordance with the definitions as set out in **Attachment I** to this letter.

We confirm that, to the best of our knowledge and belief, having made such inquiries as we considered necessary for the purpose of appropriately informing ourselves:

General:

- 1) We have fulfilled our responsibilities, as set out in the terms of the engagement letter dated September 23, 2016, for:
 - a) the preparation and fair presentation of the financial statements and believe that these financial statements have been prepared and present fairly in accordance with the relevant financial reporting framework.
 - b) providing you with all information of which we are aware that is relevant to the preparation of the financial statements, such as all financial records and documentation and other matters, including (i) the names of all related parties and information regarding all relationships and transactions with related parties; and (ii) the complete minutes of meetings, or summaries of actions of recent meetings for which minutes have not yet been prepared, of Council and committees of Council that may affect the financial statements, and providing you with access to such relevant information. All significant board and committee actions are included in the summaries.
 - c) providing you with additional information that you may request from us for the purpose of the engagement.
 - d) providing you with unrestricted access to persons within the City from whom you determined it necessary to obtain audit evidence.

- e) such internal control as we determined is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error. We also acknowledge and understand that we are responsible for the design, implementation and maintenance of internal control to prevent and detect fraud.
- f) ensuring that all transactions have been recorded in the accounting records and are reflected in the financial statements.
- g) providing you with written representations that you are required to obtain under your professional standards and written representations that you determined are necessary.

Internal control over financial reporting:

- 2) We have communicated to you all deficiencies in the design and implementation or maintenance of internal control over financial reporting of which management is aware.

Fraud and non-compliance with laws and regulations:

- 3) We have disclosed to you:
 - a) the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud
 - b) all information in relation to fraud or suspected fraud that we are aware of and that affects the City and involves: management, employees who have significant roles in internal control, or others, where the fraud could have a material effect on the financial statements
 - c) all information in relation to allegations of fraud, or suspected fraud, affecting the City's financial statements, communicated by employees, former employees, regulators, or others
 - d) all known instances of non-compliance or suspected non-compliance with laws and regulations, including all aspects of contractual agreements, whose effects should be considered when preparing financial statements
 - e) all known actual or possible litigation and claims whose effects should be considered when preparing the financial statements

Commitments & contingencies:

- 4) There are no:
 - a) other liabilities that are required to be recognized and no other contingent assets or contingent liabilities that are required to be disclosed in the financial statements in accordance with the relevant financial reporting framework, including liabilities or contingent liabilities arising from illegal acts or possible illegal acts, or possible violations of human rights legislation
 - b) other environmental matters that may have an impact on the financial statements
 - c) guarantees, whether written or oral, under which the City is contingently liable.

Subsequent events:

- 5) All events subsequent to the date of the financial statements and for which the relevant financial reporting framework requires adjustment or disclosure in the financial statements have been adjusted or disclosed.

Related parties:

- 6) We have disclosed to you the identity of the City's related parties and all the related party relationships and transactions of which we are aware and all related party relationships and transactions have been appropriately accounted for and disclosed in accordance with the relevant financial reporting framework.
- 7) We have disclosed to you all the related party relationships and transactions/balances of which we are aware.
- 8) All related party relationships and transactions/balances have been appropriately accounted for and disclosed in accordance with the relevant financial reporting framework.

Estimates:

- 9) Measurement methods and significant assumptions used by us in making accounting estimates, including those measured at fair value, are reasonable.

Going concern:

- 10) We have provided you with all information relevant to the use of the going concern assumption in the financial statements.
- 11) We confirm that we are not aware of material uncertainties related to events or conditions that may cast significant doubt upon the City's ability to continue as a going concern.

Misstatements

- 12) We approve the corrected misstatements identified by you during the audit described in **Attachment II**.

Assets & Liabilities – General:

- 13) The City has satisfactory title to all owned assets.
- 14) We have no knowledge of any liens or encumbrances on assets and/or assets that have been pledged or signed as security for liabilities, performances of contracts, etc., not disclosed in the financial statements.
- 15) We have no knowledge of any plans or interactions that may materially affect the carrying value or classification of assets and liabilities.

Contractual Agreements:

- 16) The City has complied with all aspects of contractual agreements that would have a material effect on the financial statements in the event of non-compliance including violations or default of the covenants in the City's debt agreements.

Environmental Matters:

17) The City has appropriately recognized, measured and disclosed environmental matters in the financial statements.

Non-Financial Assets:

18) We have reviewed non-financial assets, including tangible capital assets, to be held and used, for impairment, whenever events or changes in circumstances have indicated that the carrying amount of the assets might not be recoverable.

Employee Future Benefits:

- 19) The employee future benefits costs, assets and obligation, if any, have been determined, accounted for and disclosed in accordance with the financial reporting framework.
- 20) We have no knowledge of arrangement (contractual or otherwise) by which programs have been established to provide post-employment benefits, except as disclosed to you.
- 21) The significant accounting policies the City has adopted in applying PS 3255, Post-employment benefits, compensated absences and termination benefits (hereinafter referred to as "PS3255") are disclosed in the notes to the financial statements.
- 22) All arrangements (contractual or otherwise) by which programs have been established to provide post-employment benefits have been disclosed to you and included in the determination of pension and post-employment costs and obligations. This includes:
- a) pension and other retirement benefits expected to be provided after retirement to employees and their beneficiaries.
 - b) post-employment benefits expected to be provided after employment but before retirement to employees and their beneficiaries. These benefits include unused sick leave and severance benefits.
 - c) compensated absences for which it is expected employees will be paid. These benefits include accumulated sick days, and termination benefits.
- 23) The post-employment benefit costs, assets and obligation have been determined, accounted for and disclosed in accordance with PS 3255. In particular:
- a) each of the best estimate assumptions used reflects management's judgment of the most likely set of conditions affecting future events; and
 - b) the best estimate assumptions used are, as a whole, consistent within themselves, and with the valuation method adopted for purposes of this evaluation.
- 24) The assumptions included in the actuarial valuation are those that management instructed Nexus Actuarial Consultants Ltd. ("Nexus") to use in computing amounts to be used by us in determining pension costs and obligations and in making required disclosures in the above-names financial statements, in accordance with PS 3255.
- 25) In arriving at these assumptions, management has obtained the advice of Nexus, but has retained the final responsibility for them.
- 26) The source data and plan provisions provided to the actuary for preparation of the actuarial valuation are accurate and complete.

27) All changes to plan provisions or events occurring subsequent to the date of the actuarial valuation and up to the date of this letter have been considered in the determination of pension and other post-employment benefit costs.

Segment Disclosures:

28) The City's operating segments have been appropriately identified and the related segment and enterprise-wide disclosures have been made in the financial statements in accordance with the relevant financial reporting framework. The operating segment information disclosed in the financial statements is consistent with the form and content of the information used by the City's chief operating decision maker for the purposes of assessing performance and making operating decisions about the City's individual operations. All significant differences in measures used to determine segment income have been appropriately identified and described in the disclosures of segment information in accordance with the relevant financial reporting framework.

Experts / Specialists:

29) The information provided by us to Nexus, and used in the work and findings of Nexus, is complete and accurate. We agree with Nexus's findings in evaluating the accuracy and completeness of employee future benefits and have adequately considered their qualifications in determining the amounts and disclosures used in the financial statements and underlying accounting records. We did not give nor cause any instructions to be given to Nexus with respect to the values or amounts derived in an attempt to bias their work, and we are not otherwise aware of any matters that have had an impact on Nexus's independence and objectivity.

Other:

30) Expenditures will be appropriately authorized and actual expenditures will not exceed budgeted expenditures detailed in the budget bylaw.

31) We have appropriately prepared the Form C2 – Home Owner Grant: Treasurer/Auditor Certification in accordance with the financial reporting provisions of Section 12(1) of the Home Owner Grant Act.

32) We have complied with subsection 2 and 3 section 124 of Part 8 of the School Act.

33) All reserve transactions have been appropriately approved, in accordance with applicable legislation and are appropriately credited to or charged against fund balances. Reserve amounts represent only those amounts that are available for use at the City's discretion and do not include restrictions on use by third parties

34) All transfers out of statutory reserves have been conducted in accordance with the approved bylaws.

Yours very truly,

Ms. Laura Mercer, Deputy Financial Officer

Ms. Jamie Slater, Senior Accountant

cc: The Mayor and Council of the City of Nanaimo

Attachment I – Definitions

MATERIALITY

Certain representations in this letter are described as being limited to matters that are material. Misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements. Judgments about materiality are made in light of surrounding circumstances, and are affected by the size or nature of a misstatement, or a combination of both.

FRAUD & ERROR

Fraudulent financial reporting involves intentional misstatements including omissions of amounts or disclosures in financial statements to deceive financial statement users. Misappropriation of assets involves the theft of an entity's assets. It is often accompanied by false or misleading records or documents in order to conceal the fact that the assets are missing or have been pledged without proper authorization.

An error is an unintentional misstatement in financial statements, including the omission of an amount or a disclosure.

RELATED PARTIES

In accordance with Canadian public sector accounting standards (PSAB) *related party* is defined as:

- A related party exists when one party has the ability to exercise control or shared control over the other. Two or more parties are related when they are subject to common control or shared control. Related parties also include key management personnel and close family members.

In accordance with Canadian public sector accounting standards (PSAB) a *related party transaction* is defined as:

- A transfer of economic resources or obligations between related parties, or the provision of services by one party to a related party. These transfers are related party transactions whether or not there is an exchange of considerations or transactions have been given accounting recognition. The parties to the transaction are related prior to the transaction. When the relationship arises as a result of the transaction, the transaction is not one between related parties.

Attachment II - Summary of Audit Misstatements:**Corrected Audit Misstatements**

Description of misstatements greater than \$175,000 individually	Income effect	Financial position		
	(Decrease) Increase	Assets (Decrease) Increase	Liabilities (Decrease) Increase	Accumulated surplus (Decrease) Increase
To reclassify temporary investments greater than 90 days from cash and cash equivalents.				
Temporary investments	-	\$1,073,539	-	-
Cash and cash equivalent		(\$1,073,539)		
To reclassify gain on sale of certain land assets from other revenue.				
Other revenue	(\$1,289,953)	-	-	-
Gain on disposal of tangible capital assets	\$1,289,953			
Total differences	-	-	-	-

Corrected Misstatements in Presentation and Disclosure

We identified presentation and disclosure misstatements with respect to:

- The presentation of budgeted corporate service expenses in the Statement of Operations and annual budget note disclosure
- The presentation of gain/loss on disposal of tangible capital assets and proceeds from the sale of tangible capital assets in the Statement of Cash Flows
- The presentation of payments in lieu of taxes in the Schedule of Operations by Segment

Appendix 4: Management Letter

Please see attached.



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PRIVATE & CONFIDENTIAL

Ms. Laura Mercer
Deputy Financial Officer
City of Nanaimo
411 Dunsmuir Street
Nanaimo, BC V9R 0E4

April 30, 2018

Dear Ms. Mercer

Re: Reporting on Internal Control Matters

In planning and performing our audit of the consolidated financial statements of the City of Nanaimo (the "City" or the "Entity") for the period ended December 31, 2017, we obtained an understanding of internal control over financial reporting (ICFR) relevant to the City's preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances for the purpose of expressing an opinion on the financial statements, but not for the purpose of expressing an opinion on ICFR. Accordingly, we do not express an opinion on the effectiveness of the Entity's ICFR.

Our consideration of ICFR was for the limited purpose described above and was not designed to identify all control deficiencies that might be significant deficiencies and therefore, there can be no assurance that all significant deficiencies and other control deficiencies have been identified. As a result, any matters reported below are limited to those deficiencies in ICFR that we identified during the audit.

Our awareness of control deficiencies varies with each audit and is influenced by the nature, timing, and extent of audit procedures performed, as well as other factors.

Refer to the Appendices for the definitions of various control deficiencies.

SIGNIFICANT DEFICIENCIES

We identified control deficiencies that we determined to be significant deficiencies in ICFR. We report on these matters in Appendix A.

We identified a control deficiency that we determined to be an other control deficiency in ICFR that has not been communicated to management by other parties and that, in our professional judgment, is of sufficient importance to merit management's attention. We report on this matter in Appendix B.

Refer to the Appendix C for the definitions of various control deficiencies.



City of Nanaimo
April 30, 2018

Management's responses

Management's responses have not been subjected to the audit procedures applied in the audit, and accordingly, we express no opinion on them.

USE OF LETTER

This letter is for the use of management and those charged with governance in carrying out and discharging their responsibilities and should not be used for any other purpose or anyone other than management and those charged with governance. KPMG shall have no responsibility or liability for loss or damages or claims, if any, to or by any third party as this letter has not been prepared for, and is not intended for, and should not be used by, any third party or for any other purpose.

Yours very truly,

A handwritten signature in black ink that reads 'KPMG LLP'. The signature is written in a cursive, slightly slanted style. Below the signature is a horizontal line that starts under the 'K' and ends under the 'P', with a small upward tick at the end.

Chartered Professional Accountants

Nancy Adie-MacKay

Partner
(604) 691-3044

Liette Bates-Eamer

Partner
(250) 480-3641

cc:
The Mayor and Council of the City of Nanaimo

Appendix A

Significant Control Deficiencies

1. Whistleblower Policies

The City has two policies under which an employee can raise concerns:

1. Respectful Workplace
2. Reporting Serious Misconduct

The Respectful Workplace policy addresses disrespectful conduct which is defined as “any conduct or comment that is objectionable or unprofessional, which serves no legitimate work purpose and which has the effect of creating an intimidating, humiliating, hostile or offensive work environment.” The purpose of the policy is to “provide direction on what is and what is not a respectful workplace and to outline the procedures for resolving respectful workplace complaints.”

The Reporting Serious Misconduct policy establishes “a process whereby employees can report serious misconduct confidentially and without fear of retaliation, using an internal, high level communication channel.”

Both policies outline that employees are encouraged to report concerns without fear of reprisal which is a foundational concept for effective whistleblower policies. Specifically, for items raised under the Reporting Serious Misconduct policy, the policy states that the City will:

- “investigate the allegation, and if required, act on recommendations
- protect the complainant against retaliation.”

During the year, senior employees raised concerns regarding the appropriate usage of City funds and the ability to collect funds owed to the City. The initial concern appeared to be handled effectively; however, when the questionable activities resumed months later, the employees raised the issue again to several members of the Senior Leadership Team of the City. In response, disciplinary letters were placed in the complainants’ employee files.

Additionally, the Respectful Workplace policy was revised five times between January 2017 and January 2018. Three of the revisions related to the individuals designated to manage complaints.

Recommendation

The City should review the Respectful Workplace and Reporting Serious Misconduct policies to ensure the differentiation between the two policies is clear and that both policies include effective escalation mechanisms; whereby, allegations involving the Chief Administrative Officer (CAO) are reported directly to the Mayor or a revolving designate of Council. Additionally, all complaints against senior leadership team members should be reviewed by the Mayor or a revolving designate of Council. The protection from retaliation for employees who raise concerns, as outlined in the policies, must be adhered to and respected.

Additionally, these policies should be reviewed and approved by Council. Any amendments to the policies should follow the same approval process to ensure the integrity of the policies is maintained.

Management’s Response

The City will review these policies and make any necessary changes.



Appendix A

Significant Control Deficiencies

2. Expense Report Review, Authorization, and Policies

During the year, the expense reports of the CAO were being reviewed and approved by the Chief Financial Officer (CFO), a subordinate to the CAO. In following normal protocol, the CFO's expense reports were reviewed and approved by the CAO. This cross approval process provides for the opportunity of collusion between the two parties and is not an appropriate internal control.

Additionally, when discussing the review procedures performed when approving expense reports, it appears that the proper due diligence is not always followed in reviewing the items being submitted for approval.

When reviewing the supporting expense policies, we noted that the City's current policy related to Travel Guidelines is dated May 23, 2007. We understand Management has drafted enhancements and revisions to this policy that have yet to be approved.

Recommendations

We have recommended in the past, and continue to recommend, that the City's expense policy approval hierarchy be reviewed and amended to ensure that all expense reports are approved by a person more senior than the person submitting the expenses. Specifically, the CAO's expenses should be reviewed by the Mayor or a revolving designate of Council.

We also recommend that those who approve expense reports and City credit card statements are provided with guidance with respect to the duty and care required to approve an expense. Timely action must be taken in the event of non-compliance with City policies.

We also recommend the drafted revisions to the Travel Guidelines be reviewed and approved on a timely basis and that the policies incorporate our above recommendations.

Management's Response

The City has plans to review all expense policies and update where needed.

3. Consistency of Hiring Practices

The City has a well-established hiring protocol whereby job opportunities are posted, interviews are conducted, personality traits are tested for senior positions, criminal record checks are obtained, and references are verified. It appears that in some situations, steps in the process are bypassed.

Recommendation

We recommend that the hiring protocol be reviewed with certain steps being tailored for the position being filled (i.e. personality testing limited to senior positions, etc.); however, once the protocol is set, the protocol should be followed for the filling of all positions.



Appendix A

Significant Control Deficiencies

Management's Response

We agree that the City has a well-established hiring protocol whereby job opportunities are posted, interviews are conducted, personality traits are tested for senior positions, criminal record checks are obtained, and references are verified.

In some situations, steps in the process have been bypassed at the senior management level, that advice from Human Resources was not followed, and that candidates have been hired into positions without having met all the usual screening requirements.

Staff commits to adhering to the hiring protocol for all positions, and that whenever possible, selection panels will be comprised of more than one subject matter expert from the department filling the vacancy and that Human Resources be given greater consideration in hiring decisions.

4. Governance Understanding and Responsibilities

Through discussion with Senior Leadership and Council, there appears to be a lack of clarity regarding the roles and responsibilities associated with various committees, particularly the Finance and Audit Committee (the Committee). The terms of reference for the Committee are publicly available on the City website; however, the responsibilities of Council compared to the CAO are not well understood, along with other fiduciary duties.

Recommendations

We recommend that Council members partake in an education session which outlines the governance policies of the City, a review of the terms of reference for the various committees, and the roles and responsibilities for any committee chairs. The terms of reference for the committees should be reviewed on an annual basis to ensure the committees are meeting all of the requirements and that the terms are still relevant. The education session should also cover the confidentiality protocols, freedom of information procedures, and the escalation process when roles and responsibilities are not fulfilled.

Strong corporate governance which is set by senior management, the audit committee, and the board of directors (or Council for the City's context), creates the ethical climate of an organization which is often referred to as the "tone at the top". Having a strong tone at the top is important as it helps to foster an environment where fraud is deterred.

Management's Response

The City will arrange to have educational sessions with all members of the various Committees.



Appendix B

Other Control Deficiency

1. Reserves

In our review of the City's reserves, we noted that an annual budget exists for transfers to and from reserves. If circumstances occur throughout the year that require changes to planned provisions or use of reserves, transfers are made to true up results to actual or reallocate amounts within the reserves reported in the yearend financial statements with approvals for such transfers occurring subsequent to year end. Best practice would be that all approvals of changes to reserve accounts are obtained within the fiscal year.

Recommendations

We understand that Management is in the process of establishing a comprehensive Reserve Policy for the City to help facilitate the management of the City's reserves. A reserve policy would speak to adequacy of reserve levels and guidelines on use and replenishment of reserves. We support this initiative and consider it appropriate to have such a policy in place. We also recommend that any transfers and approvals between reserves occur within the respective fiscal year.

Management's Response

The City is committed to the development of a reserve policy to ensure responsible management of City funds.



Appendix C

Definitions

Terminology	Definition
DEFICIENCY IN INTERNAL CONTROL (“control deficiency”)	<p>A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis.</p> <p>A deficiency in design exists when (a) a control necessary to prevent, or detect and correct, misstatements in the financial statements is missing; or (b) an existing control is not properly designed so that, even if the control operates as designed, the control is unable to prevent, or detect and correct, misstatements in the financial statements.</p> <p>A deficiency in operation exists when a properly designed control does not operate as designed or the person performing the control does not possess the necessary authority or competence to perform the control effectively.</p>
SIGNIFICANT DEFICIENCY IN INTERNAL CONTROL (“significant deficiency”)	<p>A significant deficiency in internal control is a deficiency, or combination of deficiencies, in internal control that, in the auditor’s professional judgment, is of sufficient importance to merit the attention of those charged with governance.</p>

Appendix 5: Background and Professional Standards

Internal control over financial reporting

As your auditors, we are required to obtain an understanding of internal control over financial reporting (ICFR) relevant to the preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances for the purpose of expressing an opinion on the financial statements, but not for the purpose of expressing an opinion on internal control. Accordingly, we do not express an opinion on the effectiveness of internal control.

Our understanding of ICFR was for the limited purpose described above and was not designed to identify all control deficiencies that might be significant deficiencies and therefore, there can be no assurance that all significant deficiencies and other control deficiencies have been identified. Our awareness of control deficiencies varies with each audit and is influenced by the nature, timing, and extent of audit procedures performed, as well as other factors.

The control deficiencies communicated to you are limited to those control deficiencies that we identified during the audit.

Documents containing or referring to the audited financial statements

We are required by our professional standards to read only documents containing or referring to audited financial statements and our related auditors' report that are available through to the date of our auditors' report. The objective of reading these documents through to the date of our auditors' report is to identify material inconsistencies, if any, between the audited financial statements and the other information. We also have certain responsibilities, if on reading the other information for the purpose of identifying material inconsistencies, we become aware of an apparent material misstatement of fact.

Appendix 6: Current Developments in Public Sector Accounting Standards

Standard	Summary and implications
<p>Related Party Transactions and Inter-entity Transactions</p>	<ul style="list-style-type: none"> — Two new Handbook sections were approved in December 2014, effective for fiscal years beginning on or after April 1, 2017. — Related parties include entities that control or are controlled by a reporting entity, entities that are under common control and entities that have shared control over or that are subject to shared control of a reporting entity. — Individuals that are members of key management personnel and close members of their family are related parties. Disclosure of key management personnel compensation arrangements, expense allowances and other similar payments routinely paid in exchange for services rendered is not required. — Determining which related party transactions to disclose is a matter of judgment based on assessment of: <ul style="list-style-type: none"> • the terms and conditions underlying the transactions; • the financial significance of the transactions; • the relevance of the information; and • the need for the information to enable users’ understanding of the financial statements and for making comparisons. — A related party transaction, with the exception of contributed goods and services, should normally be recognized by both a provider organization and a recipient organization on a gross basis. — Related party transactions, if recognized, should be recorded at the exchange amount. A public sector entity’s policy, budget practices or accountability structures may dictate that the exchange amount is the carrying amount, consideration paid or received or fair value.
<p>Assets, Contingent Assets and Contractual Rights</p>	<ul style="list-style-type: none"> — Three new Handbook sections were approved in March 2015, effective for fiscal years beginning on or after April 1, 2017. — The intended outcome of the three new Handbook Sections is improved consistency and comparability. — The standard includes enhanced guidance on the definition of assets and disclosure of assets to provide users with better information about the types of resources available to the public sector entity. — Disclosure of contingent assets and contractual rights is required to provide users with information about the nature, extent and timing of future assets and potential assets and revenues available to the public sector entity when the terms of those contracts are met.

Standard	Summary and implications
Asset Retirement Obligations	<ul style="list-style-type: none"> — A new standard is approved addressing the recognition, measurement, presentation and disclosure of legal obligations associated with retirement of tangible capital assets in productive use. Retirement costs would be recognized as an integral cost of owning and operating tangible capital assets. PSAB currently contains no specific guidance in this area. The standard requires the District to record a liability related to future costs of any legal obligations to be incurred upon retirement of any controlled tangible capital assets (TCA). — An ARO liability is initially recorded at its fair value (normally estimated using a present value technique), at the time of acquisition or construction of the TCA. The liability is subsequently increased or “accreted” up to the settlement date using an effective interest rate (normally the rate used to estimate the present value of the liability), with the corresponding debit amount being expensed. — A corresponding addition to the carrying amount of TCA is recognized at the same time as the ARO liability, which is then amortized over the TCA’s useful life. The net effect is an increase in TCA and ARO liability upon recognition, and over time, an increase in amortization expense and accretion expense. If the TCA is no longer in use, the amount of the ARO is expensed immediately. — The ARO standard requires the public sector entity to record a liability related to future costs of any legal obligations to be incurred upon retirement of any controlled tangible capital assets (“TCA”). The amount of the initial liability would be added to the historical cost of the asset and amortized over its useful life. — As a result of the new standard, the public sector entity has to: <ul style="list-style-type: none"> • consider how the additional liability will impact net debt, as a new liability will be recognized with no corresponding increase in a financial asset; • carefully review legal agreements, senior government directives and legislation in relation to all controlled TCA to determine if any legal obligations exist with respect to asset retirements; and • begin considering the potential effects on the organization as soon as possible to coordinate with resources outside the finance department to identify AROs and obtain information to estimate the value of potential AROs to avoid unexpected issues. — The new standard has an effective date of April 1, 2021.
Financial Instruments	<ul style="list-style-type: none"> — New accounting standards, Financial Instruments PS3450 and Foreign Currency Translation PS2601 have been approved by PSAB and are effective for years commencing on or after April 1, 2019. Early adoption is permitted. — Equity instruments quoted in an active market and free-standing derivatives are to be carried at fair value. All other financial instruments, including bonds, can be carried at cost or fair value depending on the public sector entity’s choice. This choice must be made on initial recognition of the financial instrument and is irrevocable. Instruments denominated in foreign currencies must be adjusted to reflect the exchange rate in effect at the reporting date. — A new statement, the Statement of Re-measurement Gains and Losses, will be included in the financial statements. Unrealized gains and losses incurred on fair value accounted and foreign currency denominated financial instruments will be presented in this statement. Realized gains and losses will continue to be presented in the Statement of Operations.

Appendix 7: KPMG's Cyber Security Protocol

This summary is intended to provide management and Audit Committee members with some insight into KPMG's strategies and procedures regarding our cyber defence.

KPMG Global

KPMG Global provides managed security services for member firms which includes 24x7 monitoring and alerting services to identify potential attacks on our environment. We use a series of centrally managed firewalls among our network of member firms to identify and address potential attacks to member firms and to prevent attacks from spreading between member firms. This approach was in place during the Wanna Cry outbreak and was a critical element in our successful defence against that incident.

KPMG Global has also implemented enhanced email protection to address malware and attacks through email and we have implemented automated vulnerability detection services. This service scans equipment that is exposed to the Internet and identifies known vulnerabilities on a real-time basis. "Good housekeeping" is a central tenet of our approach and we continue to focus on known vulnerabilities and patching.

KPMG Global believes the cloud represents a secure environment when appropriately configured and monitored as a platform to deliver services. Our approach to secure the cloud includes deploying full-time, dedicated security and privacy resources, integrating the cloud platform into our managed security services to promote "good housekeeping," and deploying a continuous monitoring plan for each of the cloud platforms that we deploy to member firms and to our clients.

KPMG Global has invested heavily in enhancing the security of our environment, evidenced by the introduction of our Global Security Operations Centre, managed services and other enhancements to our cyber defence.

KPMG Canada Approach

- KPMG Canada does not currently use Office 365 or Cloud based email.
- Cloud environments provide robust security when properly configured, with proper password management.
- The Canadian firm's email servers are hosted in Canada and controlled and managed by KPMG Canada.
- In compliance with our global security controls, we enforce strong passwords that need to be renewed at regular intervals.
- We also maintain a specific IT security platform for the maintenance and management of privileged accounts.
- KPMG's Information Security Program is built on a comprehensive framework of policies, standards, and processes based on ISO 27001:2013.
- KPMG's security requirements are set out in Global Information Security Policies and Standards (GISP).
- The Canadian firm undergoes an internal audit every year to ensure compliance to key security controls in the GISP.
- Every three years, the Canadian firm goes through a Compliance Review conducted by a team from non-Canadian member firms.

Appendix 8: Audit Trends

KPMG understands the wide range of challenges and evolving trends that you face as an audit committee of the City. We also understand that sometimes keeping up with critical issues as they emerge can be difficult.

As your auditors, it is incumbent upon us to provide you with any information that will help you further strengthen corporate governance, enhance your oversight and add greater value within your organization.

As such, KPMG's Audit Committee Institute ([ACI](#)) provides information, resources and opportunities for you to share knowledge with your peers. First, you are welcome to attend our Audit Committee Roundtable sessions, which are held in major cities across the country. In addition, you will also benefit from our monthly [Audit Point of View](#) article series as well as [thought leadership](#) and insights on the most pressing audit committee agenda items.

More information on all of these can easily be found at www.kpmg.ca/audit.

Our discussions with you, our audit opinion and what KPMG is seeing in the marketplace—both from an audit and industry perspective—indicate the following is specific information that will be of particular interest to the City. We would, of course, be happy to further discuss this information with you at your convenience.

Thought Leadership	Overview	Links
Audit Trends	With a range of provocative data, insight and opinion gleaned from KPMG professionals and The Conference Board of Canada survey of Audit Committees and CFOs, Audit Trends examines seven key issues addressing corporate readiness, preparedness and priority in a volatile business environment.	Link to report
The Blockchain shift will be seismic	Blockchain technology is a focused disruptor of the very foundations of external and internal audit: financial recordkeeping and reporting. This Audit Point of View article offers insight on how blockchain technology is impacting business and what audit committees should be thinking about to prepare for certain risks.	Link to article
Audit Quality 2017	Learn about KPMG's ongoing commitment to continuous audit quality improvement. We are investing in new innovative technologies and building strategic alliances with leading technology companies that will have a transformative impact on the auditing process and profession. How do we seek to make an impact on society through the work that we do?	Link to report

kpmg.ca/audit



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